Business Law Section Newsletter

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Message from the Chair

by Robert A. Kaye

Several exciting things have happened within the Business Law Section since the last issue of the newsletter.

Governor Chris Christie signed into law the Revised Uniform Limited Liability Company Act (RULLCA) on Sept. 19, 2012. It has been codified as N.J.S.A. 42:2C-1 *et seq*. RULLCA is the culmination of years of devoted service by our Business Entities Committee, led by co-chairs Ira B Marcus and Denise Walsh. They and the committee deserve the thanks of all business lawyers for helping to modernize our statute. RULLCA becomes effective on March 18, 2013. In the coming months, there will be many Institute for Continuing Legal Education (ICLE) and other seminars presented that will educate us on the important changes this law provides.

Also, I am pleased to announce the winners of the first Business Law Section Writing Competition. Our section, under the leadership of immediate past chair Gianfranco Pietrafesa, developed the concept of conducting a writing competition focused on business law issues. He gained the support of the three New Jersey law school deans, with a winner to be chosen from each school. While we were disappointed that no entries were received from Rutgers-Newark, multiple entries were received from Rutgers-Camden and from Seton Hall Law School. A panel of volunteer judges was enlisted who graded all entries on an anonymous basis. The winners are: Yasmine N. Fulena of Seton Hall, class of 2014; and John Shindle of Rutgers-Camden, class of 2013. The winners' articles are published in this issue of the newsletter, they will be invited to attend a meeting of the section's Board of Directors, and they will be awarded copies of three business law publications donated by ICLE, New Jersey Law Journal Books and Gann Law Books. Congratulations to the winners.

As a reminder, our section offers many excellent benefits. These include:

- This very fine newsletter, published several times each year, offering informative articles on a variety of topics of interest to business lawyers;
- Sponsorship of mandatory continuing legal education programs throughout the year, including Brown Bag Luncheon Webinars and the day-long Business Law Symposium;

- Holding joint meetings with other sections, such as tax and labor and employment;
- The CommunityNet on the state bar association's website, where members may solicit views from or offer worthy information to fellow practitioners;
- Support for the Inns of Transactional Counsel that currently operate in the Morris-Essex and Hudson-Bergen areas; and
- A variety of committees devoted to particular areas of interest to the business bar, including labor, intellectual property, environmental, health and other topics.

As with any organization, the benefits derived are made possible by the support and contributions of its members. Please take a moment to consider how you may be able to get more from your membership. Write an article for the newsletter, join a committee, become a presenter or panelist at one of our programs, join an inn of court.

I and my predecessors recognize that the strength of our section is due in large part to the diversity of our membership, and I remain committed to expanding that diversity to ensure our section reaps the benefit of the full spectrum of knowledge and experiences provided by a diverse membership.

We constantly strive to better serve our members and potential members. If you have ideas you would like to share, please contact me at 201-348-6000 or rkaye@chasanlaw.com. ■

Notes From the Editors

by Denise Walsh, Edward Sturchio and Thomas Zalewski

Seasons greetings. We are pleased to bring you this edition of the *Business Law Section Newsletter.*

This edition includes articles spanning a range of topics and disciplines. Articles included in this edition cover a view of the practice of law from a solo practitioner's perspective, key issues for employers of telecommuters, insight into the regulatory complexities of private investment funds and a thoughtful piece on the benefits of women serving on corporate boards. We are indebted to all authors for their contributions, and hope you find these articles to be informative and helpful for your practice.

Also included in this edition are the winning entries from the Business Law Section's inaugural Business Law Student Writing Competition, along with a forward by Gianfranco A. Pietrafesa, an esteemed member of the Business Law Section's Board of Directors and a driving force behind the competition. We congratulate the winning contestants and thank all who volunteered their time to ensure the competition's successful launch. We look forward to the competition's continued success in the future.

As always, we are interested in hearing from you, the readers, about topics you would like to see addressed in future editions of the newsletter. Please feel free to reach out to any of us with suggestions.

Call for Articles

We are seeking articles for the spring 2013 issue of the *Business Law Section Newsletter* on topics of interest to business lawyers in New Jersey.

The deadline for submitting articles for the spring 2013 edition is April 15, 2013.

Interested in submitting? You can contact any of the editors at:

Ed Sturchio at 973-966-8243 or esturchio@daypitney.com
Denise Walsh at 973-740-1200, ext. 608 or dwalsh@marcusbrodylaw.com
Tom Zalewski at 973-966-8115 or tzalewski@daypitney.com

We look forward to hearing from you.

Inside this issue

Solo Practice: A Balancing Act

by Sheryl Bernstein Cilenti

According to the Office of Attorney Ethics, a majority of lawyers in private practice in New Jersey are practicing as solo practitioners or in a small law firm environment.[1] Even more pronounced is that almost three-quarters of all private law firms in New Jersey operated as solo law firms during the past year.[2] In a solo practice, the attorney is the practicing attorney—performing legal services; the office manager—taking care of administrative items; the rainmaker—finding and keeping clients; and the connection to the community—providing *pro bono* services and controlling the firm's public relations.

For some attorneys, solo practice is their only experience in the field of law. For other attorneys, solo practice is just one of many experiences during a long career. Whether an attorney is coming from a large law firm, a corporate counsel position, or straight from law school graduation, starting and maintaining a solo law practice in an organized and thoughtful manner will aid in its success.

Regardless of the reasons behind the creation of a solo practice, such as the desire for autonomy and decision-making power, the need to harmonize work and life circumstances or the unfortunate result of a layoff, all attorneys in solo practice face the same balancing act. An attorney engaged in solo practice must be able to balance the internal needs of the firm, consistently seek to build and sustain a meaningful practice, and find the necessary time and a good fit for *pro bono* and community service.

As a general business principle, it is important for all attorneys to produce the best possible legal work under the circumstances. Producing sloppy, inconsistent and faulty work product will not only lose clients, but will tarnish a practitioner's reputation and have lasting negative effects. For a solo practitioner, it is even more critical to consistently provide top-quality legal work and practical, real advice for clients. In some larger firms, attorneys may review and edit each other's work product, or even have strict oversight requirements, but a solo practitioner does not have those resources. In addition, in larger firms multiple attorneys may be providing legal services to the same client at the same time, and can coordinate the presentation of work product and support each other's efforts. A solo practitioner does not have the same support system, and will instead need to produce the work and then also review, proof and correct the final product without input from other firm attorneys before it is submitted to the client. For a solo practitioner in particular then, thoroughness and attention to detail are indispensable skills.

Some corporate solo practitioners make the mistake of trying to be a jack of all trades for their clients. Instead, a commercial business lawyer with little or no litigation experience must find other ways to service a client that asks for assistance with a complex litigation matter or other request outside of the general corporate area. In such circumstances, it is wiser to seek co-counsel or to refer the matter to a reliable attorney experienced in the applicable type of litigation or area of law rather than either: 1) producing a low-quality complaint or other core document that may leave out essential claims or defenses (thus potentially barring the client in the future), or 2) spending an enormous amount of time learning the basics of litigation or other area of law only to be forced to write the time off or charge an unreasonably high amount for the service provided.

Focusing on core strengths and providing other ways to help satisfy client needs builds an overall stronger legal practice. A solo law practice needs to continually build its client roster to remain a viable firm, so turning away a client or an individual matter from a client, even if the client is directed to an alternative solution, takes an enormous amount of restraint on the part of most solo practitioners. When faced with the difficult decision of whether or not to provide a type of legal service outside of one's specialty area, a solo practitioner must be conscious that a satisfied client is a returning and lasting client, whereas a client who receives inferior or unreasonably expensive advice may end up costing an attorney more in the future.

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A solo practitioner must also be mindful to run his or her firm as a business, and not treat it like a hobby. Running a firm as a business includes keeping the office organized in terms of billing, expenses and communications. It is difficult, but being disciplined will strengthen a firm. For instance, setting a time frame, such as the first week of every month (yes every month), to get the firm's billing out will help with cash flow. Once the invoices are sent, it is important to follow up with clients and possibly negotiate or offer different payment options as circumstances may warrant. A solo practitioner must also make it a priority to return phone calls and emails within 24 hours, even when the return message is only to set up a time to talk at a later date. Striving to make every client feel like the firm's most important client is a worthwhile effort that will help clients feel valued. Generally, maintaining a client is less costly and takes less time than acquiring a new client.

In addition to providing superior legal services and running the practice like a business, solo practitioners also need to focus on building and maintaining their practice. Finding time to grow a client base is an issue that plagues many solo practitioners. Such practitioners find themselves so inundated with running their firm and managing the workload, that they put networking at the bottom of the list. Instead, solo practitioners should build networking time into their daily, weekly or monthly schedules. Networking does not have to be a scary endeavor. A networking activity can be as simple as reaching out to an old colleague or attending a meeting of a local business association. The strongest way to build a network is to take the time to learn about an individual's or a company's needs and help the potential client find viable solutions to fulfill those needs, legal or non-legal.

Networking can happen anywhere, including seminars, continuing legal education events, the gym, a school-related function, or even a holiday party. Networking does not mean working a room, carelessly handing out business cards and reciting a pre-rehearsed elevator pitch. It means listening and understanding what is important to the people in the broad community. Once an attorney understands the unique situation of a potential client, the practitioner can offer some background on his or her skills and connect the individual with applicable resources in the potential client's field of interest. Sometimes a practitioner's efforts will result in an immediate paying opportunity, but more importantly the practitioner will have made a connection and broadened his or her long-term network. It also may lead to meaningful *pro bono* opportunities, or even future networking possibilities. Creating time to network on a regular basis will assist solo practitioners in maintaining and growing a strong firm.

At its basic core, a successful solo practice requires clients. Networking, referrals and word of mouth can all assist a solo practitioner in identifying potential new clients. However, clients come in all shapes and sizes, and some are not right for a small firm. Based on the limited number of hours a solo practitioner has to offer, potential clients need to be vetted for both ability to pay and conflicts, as well as an overall fit with the practitioner's culture. When a solo practitioner is vetting clients it is important to pay attention to gut feelings or instincts, as the solo practitioner is the only one deciding if the client is a good fit. Once the decision has been made to accept a client, and the engagement process is complete, maintaining contact is vital to a successful relationship. Providing necessary updates and producing work when promised are keys to cultivating a satisfied client. Further, it is beneficial to stay in touch with clients even when not directly performing work for them. It gives a practitioner the ability to stay connected with a client's needs, to understand what changes have occurred in the client's business, and to remain a top-of-mind resource.

Being a solo practitioner can also seem isolating at times, so it is necessary to continue to maintain and build a relationship with other professionals, including previous employers, co-workers, and local businesses. Interacting and staying connected with the surrounding legal community helps combat isolation and fosters a sense of shared goals and identity. Generally, a solo practitioner does not have the ability to walk down the hall and connect with his or her peers. Instead, a solo practitioner should create a network or group of other attorneys in various complimentary fields, which for a business attorney may include tax, estate planning, bankruptcy, and litigation. It is also helpful to create and foster a network of attorneys in one's personal area of expertise. The network of attorneys can be comprised of other solo practitioners or attorneys that are part of larger firms. Within such a network, solo practitioners can give and get referrals, provide a sounding board for each other, provide backup services when necessary and share common experiences—all of which are important functions that are more generally found in larger law practices.

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Lastly, solo practitioners should get involved in their communities, *pro bono* activities and other public service initiatives. These activities provide non-monetary rewards that in the words of MasterCard® are "priceless." Corporate lawyers may feel uncomfortable providing *pro bono* services if they believe that *pro bono* work only involves litigation matters. Fortunately, however, many corporate and commercial *pro bono* opportunities exist.

For a *pro bono* experience to be memorable, and one an attorney desires to repeat, a solo practitioner should get involved with things that are meaningful to him or her, and to his or her family and friends. There are many examples of areas where corporate lawyers can add significant value. For example, local educational organizations like parent-teacher organizations or education foundations can use a solo practitioner's services to review contracts and evaluate agreements. Local organizations that hold fundraisers also need help negotiating contracts with the venues for their events (such as hotels, meeting halls and catering facilities) and with the service providers for their events. They also need help reviewing insurance policies and press releases. Cultural organizations can use help with formation activities (especially if the practitioner has experience forming 501(c)(3) organizations) or reviewing and updating bylaws. Many of these types of organizations also need assistance in negotiating leases. Further, if an attorney has transactional experience, he or she may be connected with local businesses and organizations (including nonprofit, charitable and religious organizations) seeking to merge or acquire other entities.

It is surprising how many organizations will sign contracts or agreements without any legal review, and how inspiring and rewarding it can be to assist an organization in need. As a corporate attorney it may seem more difficult to come across *pro bono* opportunities in one's area of expertise, but the environment has broadened and evolved to include a wide variety of initiatives. In addition to finding *pro bono* opportunities on an individual basis, there are various organizations throughout New Jersey and the country that match attorneys to individuals of need, or charitable, religious, civil community, government or educational organizations.[3]

One *caveat*, before beginning any legal *pro bono* work, solo practitioners should confirm legal malpractice coverage. Many lawyers' professional liability policies provide coverage for *pro bono* work performed by covered lawyers (such that an existing policy may cover *pro bono* legal services as well as traditional legal services performed by covered attorneys). In addition, some charitable and nonprofit organizations provide malpractice insurance coverage for their volunteers, but the coverage is based on certain factors. Either way, it is critical to determine malpractice insurance coverage prior to providing legal *pro bono* services.

Practicing law as a solo practitioner involves the balancing of a variety of important functions. It is easy to get caught up in one aspect, but over time, the more successful attorneys find a way to provide meaningful attention to balancing the internal needs of running a business with building a practice and connecting with their community.

Sheryl Bernstein Cilenti is a solo practitioner in Madison. She focuses on serving the commercial and corporate legal needs of small to medium-sized companies and entrepreneurs, with an emphasis on general business matters, commercial transactions, mergers and acquisitions, corporate governance issues and employment-related matters.

Endnotes

1. 2011 State of the Attorney Disciplinary System Report, Office of Attorney Ethics.
2. *Id.*
3. For example, the New Jersey State Bar Association website contains a list of organizations providing *pro bono* opportunities.

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What Business Owners Should Know About Telecommuters

by Alix R. Rubin

With the advent of sophisticated mobile and remote computer technology, the frequency of such natural disasters as Superstorm Sandy and business efforts to go 'green,' cut costs and achieve work-life balance, telecommuters are becoming more and more prevalent in the workforce. Although federal government offices in Washington, D.C. were closed for two days during Sandy, about one third of government workers continued working remotely. Under the Telework Enhancement Act,[1] federal agencies are required to implement telework policies. According to the U.S. Census Bureau, more than 13 million U.S. residents, approximately 9.5 percent of all U.S. workers, work from home at least one day a week.

Employers increasingly recognize the need and desire for employees to be able to work from anywhere. However, business owners should consider the following questions that may arise when employees telecommute:

- What impact does telecommuting have on the payment of wages under the Fair Labor Standards Act[2] and the New Jersey Wage and Hour Law?[3]
- When is telecommuting a reasonable accommodation under the Americans with Disabilities Act[4] and the New Jersey Law Against Discrimination?[5]
- Are business owners required to pay taxes and carry workers' compensation insurance in other states from where their employees telecommute?

Other issues that will not be discussed in this article, but that business owners who permit telecommuting should also address, include family and medical leave, employee privacy, confidential and proprietary business information, workplace safety and zoning.

Wage and Hour Issues

A significant concern for employers is how to properly report, record and monitor the time worked by non-exempt telecommuters—those who do not qualify as executive, administrative, or professional employees or outside salespeople exempt from overtime under the Fair Labor Standards Act and the New Jersey Wage and Hour Law. Employers should require non-exempt telecommuters to 'clock' in and out via a time reporting system (cloud-based or accessible remotely), email or telephone. In addition, a policy that requires prior written management approval to work overtime will help reduce the amount of overtime clocked.

To avoid discrimination claims, such a policy must be enforced for all non-exempt employees, not just telecommuters. While an employee may be disciplined for failing to receive prior written approval to work overtime, all hours worked over 40 in any given week still must be paid at time and a half.

Non-exempt telecommuters may also need to be paid for time and travel to and from their home base—but not to the main office—provided most of their working hours are from that base. In addition, any 'on-call' time is compensable if the employee cannot use that time effectively for personal pursuits.

To avoid off-the-clock wage and hour violations, business owners also need to monitor, and perhaps even limit, the after-hours business use of such company-issued electronic devices as smartphones and remote access by non-exempt employees who work primarily at the company's office.

Is Telecommuting a Reasonable Accommodation?

New Jersey courts have not directly addressed under what circumstances, if any, telecommuting may be a reasonable accommodation under the Americans with Disabilities Act (ADA) and the New Jersey Law Against Discrimination. Under both statutes, employers are required to reasonably accommodate disabled employees, unless the accommodation imposes an undue hardship. In addition, failure to accommodate an employee with a disability constitutes unlawful discrimination.

The Federal Equal Employment Opportunity Commission (EEOC) and federal courts in such states as New York, Ohio, Michigan and Illinois have held that telecommuting may be a form of reasonable accommodation. For example, the Second Circuit held that allowing a hearing-impaired employee who also suffers from cancer, heart problems and asthma to work from home was one of several options the employer should have considered as a reasonable accommodation to assist in her commute to work.[6] Among the factors to be assessed in this individualized analysis was "the reasonableness of allowing [the employee] to work without on-site supervision."[7]

More recently, however, in *Core v. Champaign County Board of Comm'rs*, the Southern District of Ohio ruled against an employee who requested to work from home as a reasonable accommodation to her asthma and sensitivity to perfume, because she could not perform all of the essential functions of her job at home.[8] Notably, the plaintiff's position required her to meet with clients, inspect in-home daycare facilities, conduct and attend training sessions, and maintain a database and physical files accessible only at her worksite. However, quoting Sixth and Seventh circuits' precedent, the court acknowledged that there might be exceptions "in the unusual case where an employee can effectively perform all work-related duties at home."[9]

Citing the same Sixth and Seventh circuits' precedent, which are now 15 and 17 years old, respectively,[10] in *EEOC v. Ford Motor Co.,* the Eastern District of Michigan opined that "working at home is rarely a reasonable accommodation" because "regular attendance is a basic requirement of most jobs."[11] In this case, the court found that a resale buyer's request to work from home up to four days a week due to her irritable bowel syndrome was not a reasonable accommodation because her role often required face-to-face interaction, and did "not lend itself to frequent, unpredictable workdays out of the office."[12] The court declined to second-guess the employer's "reasoned business judgment" regarding what constituted the essential functions of the plaintiff's job.[13]

In light of the technological advances that have occurred during the last 17 years or so, in *Bixby v. JP Morgan Chase Bank*, the Northern District of Illinois held that working from home accommodations are not "per se unreasonable, and courts must look to the particular facts and circumstances of the case to determine whether such an accommodation is proportional to costs."[14] Here the job duties of a project manager—emailing, participating in teleconferences and working on his computer—lent themselves to telecommuting. The court held that a reasonable jury could find working from home to be a reasonable accommodation for the plaintiff, who suffered from various psychological disorders, because his employer allowed other project managers to work from home on a full-time, permanent basis. Therefore, the court denied the employer's motion for summary judgment on the plaintiff's ADA failure to accommodate claim.[15]

As early as 1999, the EEOC has supported telework as a reasonable accommodation. The agency's most recent guidance on this subject is already seven years old, and does not yet incorporate the ADA Amendments Act[16] that went into effect in Jan. 2009. Nonetheless, the guidance is instructive to business owners faced with an employee's request to work from home as a reasonable accommodation.

Following are significant takeaways from the EEOC guidance, as well as the limited case law cited above:

- Employers are not required to offer telework to all employees. However, if some employees are allowed to work from home, business owners must give employees with disabilities an equal opportunity to do so.
- Employers may have to waive certain eligibility requirements for telework for a disabled employee who needs to work from home. These may include such threshold requirements as employment with the company for at least one year and no negative performance reviews, or restrictions on the number of days per week an employee may telework.
- Even if the business owner does not currently have a telework program in place, working from home may be a reasonable accommodation for a disabled employee.
- As with any requested accommodation, the employer must engage in an individualized 'interactive process' with the disabled employee to determine whether telework—on a full-time or part-time basis—will enable the employee to perform the job, and whether this accommodation imposes an undue burden on the employer.
- Up-to-date job descriptions that include the essential functions of the position are key to the ability to determine whether a particular job can be performed at home. Essential functions do not have to be changed to enable the employee to telework.
- Such factors as adequate supervision; use of specialized equipment or tools; and whether there is a need for in-person interaction, coordination

with other employees and immediate access to information located only in the workplace all play a role in determining whether telework is a reasonable accommodation for a particular employee.

Tax Liabilities

Most business owners are aware that, with a few exceptions,[17] they are required to withhold state income tax, as well as disability and unemployment insurance payments, from their employees' paychecks and pay these withholdings to the state where the employee works, or to more than one state based on the proportion of time spent working in each state. Therefore, if an employee telecommutes from another state, these withholdings must be paid to that state.

Earlier this year, New Jersey's Appellate Division added a new wrinkle. In *Telebright Corp. v. Dir., N.J. Div. of Taxation*, the Appellate Division held that a Maryland-based company that permitted one of its employees to telecommute full time from her New Jersey residence was doing business in New Jersey, and therefore subject to the New Jersey Corporation Business Tax.[18] This one employee's production of computer code in New Jersey for use in the company's web-based service constituted sufficient "minimum connection" with the state to permit taxation consistent with the due process clause of the U.S. Constitution, the court held.[19] It also rejected the company's argument that taxing businesses on the basis of their employees' remote work locations created an undue burden on interstate commerce in violation of the commerce clause.[20] In addition, the court found the fact that this employee worked from a home office rather than a company location immaterial.[21]

The key determinative factor in *Telebright* appears to be that, although the telecommuter had no contact with the company's customers, the software code she created in New Jersey was used in the company's products. Had she merely performed administrative or other "back office" duties in New Jersey, the court may have held that no taxable nexus existed.

While this decision affects out-of-state businesses rather than New Jersey companies, it may have set a precedent other states will follow. In fact, according to The Bureau of National Affairs, Inc.'s (BNA) 2012 Survey of State Tax Departments, 35 states reported that an employee who telecommutes to an out-of-state employer from a home within their borders could trigger nexus sufficient to warrant liability for state corporate business tax.[22] Therefore, business owners in New Jersey should research the tax laws of other states from where their employees may telecommute. Tax liabilities in other states may offset the savings in travel expenses and office space telework provides.

Workers' Compensation Issues

As indicated by New Jersey's Appellate Division in *Chaverri v. Cace Trucking Inc.,* most state workers' compensation laws, including New Jersey's, cover work-related injuries that occur at the employer's physical location, as well as at a telecommuter's home office or other work location.[23] In *Chaverri*, the employee's eye injury, which occurred while he performed maintenance at home on the tractor-trailer he used for work, occurred during the scope of his employment, and was therefore compensable.[24]

Nonetheless, it may be more difficult to determine whether an injury that occurred in a home office is compensable, as there may not be any witnesses to the incident, and the lines between work-related and non-work-related activities may be blurred. Establishing written policies on what constitutes a telecommuter's work activities and working hours will help keep these lines clear. In addition, specifying that a single room in the telecommuter's house be used as the home office will avoid the problem of an injury that occurs in another part of the house being claimed as compensable.

In addition, business owners must carry workers' compensation insurance in every state from which their employees telework. While many states accept 'all states' endorsements on workers' compensation policies, not all states do. For example, New York requires a separate policy endorsement. Even if the likelihood of work-related injury is minimal, accidents happen. In addition, most states levy substantial penalties for not having workers' compensation coverage, regardless of whether a compensable injury has occurred.

Conclusion

The demand for more flexible work arrangements continues to grow, as does the need for businesses to reduce their costs and environmental footprint. Telework may be the answer, provided business owners are prepared to meet the legal challenges of working offsite. Having in place a telework policy that addresses the salient issues, enforcing the policy in a nondiscriminatory manner, and following the best practices discussed above will help businesses effectively manage the legal risks.

Alix R. Rubin founded Alix Rubin Law, LLC, in 2010, providing legal counsel for both employers and employees, and also conducts internal workplace investigations of employee misconduct through Verita, LLC, and is counsel to Mandelbaum Salsburg, P.C.

Endnotes

1. 5 U.S.C. §§ 6501-6506.
2. 29 U.S.C. §§ 201 *et seq.*
3. N.J.S.A. §§ 34:11-56a to -56a38.
4. 42 U.S.C. §§ 12101 *et seq.*
5. N.J.S.A. §§ 10:5-1 *et seq.*
6. *Nixon-Tinkelman v. N.Y. City Dep't of Health & Mental Hygiene*, No. 10-3317-cv, 2011 WL 3489001, at *20 (2d Cir. Aug. 10, 2011).
7. *Id.*
8. *Core v. Champaign County Bd. of County Comm'rs*, No 3:11-cv-166, 2012 WL 4959444, at *5 (S.D. Ohio Oct. 17, 2012).
9. *Id.*
10. *Smith v. Ameritech*, 129 F.3d 857 (6th Cir. 1997); *Vande Zande v. Wis. Dep't of Admin.*, 44 F.3d 538 (7th Cir. 1995).
11. *EEOC v. Ford Motor Co.*, No. 11-13742, 2012 WL 3945540, at *5, *6 (E.D. Mich. Sept. 10, 2012).
12. *Id.* at *6, *7.
13. *Id.* at *6.
14. *Bixby v. JP Morgan Chase Bank*, No. 10 C 405, 2012 WL 832889, at *10 (N.D. Ill. March 8, 2012).
15. *Id.* at *11.
16. P.L. 110-325, Sept. 25, 2008.
17. For example, New York taxes all wages of nonresidents who telecommute part-time for a New York employer, and Georgia taxes all income earned from Georgia-based employers, regardless of whether the employee telecommutes from another state or not.
18. *Telebright Corp. v. Dir., N.J. Div. of Taxation*, 424 N.J. Super. 384, 388 (App Div. 2012).
19. *Id.* at 392.
20. *Id.* at 394-95.
21. *Id.* at 395.
22. Nadine Gjurich, "Case Study: State Tax Policies Discourage Firms From Offering Telecommuting Option," from Weekly State Tax Report, Bloomberg BNA, Oct. 18, 2012, http://www.bna.com/case-study-state-n17179870351/.
23. *See, e.g., Chaverri v. Cace Trucking Inc.*, No. A-3619-07T2, 2010 WL 1189768, at * 3 (App. Div. March 26, 2010) ("[A]n at-home injury to a telecommuter or other home-based employee is in the course of the employment if the injury occurs while business activity is actually being carried on....")
24. *Id.*

Private Fund Developments

by Charles V. Quinn

As a result of the financial crisis of 2008 and its continuing repercussions, several measures have recently been enacted affecting private funds, their advisers, and securities generally. Most importantly for private funds, recent legislative and regulatory actions have repealed the "private adviser exemption" of the Investment Advisers Act, under which many advisers to private funds, private equity funds and venture capital funds found exemption from investment adviser registration and the corresponding legal and regulatory requirements for registered advisers. In addition, a recent Securities and Exchange Commission (SEC) regulatory proposal requires advisers to many of these private funds to file periodic reports and to disclose private fund information to the government.

Because even the final regulations have been newly enacted, and revisions and legal challenges are possible, the situation is still fluid, and any description is therefore subject to further developments. Moreover, the main reporting requirements are being phased in over a period of the next several months. Nevertheless, private funds and their advisers need to be aware of these requirements and several additional proposals *now*, and to be prepared to deal with a new and, in the minds of some, a more intrusive and burdensome regulatory regime.

Provisions of the Dodd-Frank Act

Among the many changes to the regulation of the financial sector enacted into law in July 2010, Chapter 4 of the Dodd-Frank Act, titled the Private Fund Investment Advisers Registration Act of 2010 (PFIARA), focuses on investment advisers and private funds and alters the present regulatory scheme in several important ways.

Section 402 of the PFIARA amends Section 202(a) of the Investment Advisers Act of 1940 by adding the definitions of "private fund" and "foreign private adviser." A private fund is defined as an entity that would meet the definition of "investment company" under the Investment Company Act of 1940 but for the exemptions set forth in Section 3(c)(1) regarding private companies with fewer than 100 investors or Section 3(c)(7) regarding private companies containing only "qualified purchasers"[1] as set forth in the Investment Company Act. A foreign private adviser is defined as an investment adviser having no place of business in the U.S., fewer than 15 U.S. clients and investors in private funds, and aggregate assets under management attributable to U.S. clients and U.S. investors in private funds of less than $25 million. The adviser must also refrain from holding itself out generally to the public in the U.S. as an investment adviser, and may not act as investment adviser to any investment company or business development company registered under the Investment Company Act. These definitions are important, as the PFIARA changes the present regulatory scheme and adds reporting requirements for these private funds, exempting only foreign private advisers.

Specifically, Section 403 of the PFIARA amends the existing exemption from registration requirements for investment advisers under Section 203(b) of the Investment Advisers Act to exclude private fund advisers from the "local adviser" intrastate exemption and to remove the exemption from registration for those who have advised fewer than 15 clients in the past 12 months, replacing those provisions with an exemption for foreign private advisers only.

In partial replacement of these repealed provisions, the PFIARA adds more narrowly tailored exemptions for persons or entities already subject to government regulation under other laws. Section 403 adds an exemption for those registered as commodity trading advisers with the Commodity Futures Trading Commission and advising a private fund (provided that the adviser does not engage in providing securities-related advice as a predominant business) and for those who solely advise small business investment companies under the Small Business Investment Act of 1958. In addition, Section 409 of the PFIARA sets forth an exemption to the definition of "investment adviser" under the Investment Advisers Act for any "family office" to be defined by rule, regulation, or order of the SEC,[2] codifying the previous exemptive policy achieved through seeking and obtaining orders on a case-by-case basis. These exemptions, however, are not expected to be applicable to the vast majority of private investment funds currently operating in the financial markets.

In addition, Sections 407 and 408 of the PFIARA, respectively, exempt from reporting requirements advisers to "venture capital funds" and private fund advisers with assets under management in the U.S. of under $150 million. In defining the term venture capital fund, the newly enacted Rule 203(l)-1 under the Investment Advisers Act[3] focuses on the relative lack of leverage used (limiting debt generally to an amount equal to no more than 15 percent of the fund's assets and a non-renewable term of 120 days) and the non-public, startup nature of the entities in which the fund invests. The regulation allows up to 20 percent of "non-venture" investments in such funds, but also requires that investors not be given the general rights of repurchase or withdrawal common to many private funds. Furthermore, the SEC is empowered to prescribe such recordkeeping and reporting requirements as it deems necessary, among other things, to address systemic risk. Section 408 of the PFIARA also directs the SEC to consider the "size, governance and investment strategy" of "mid-sized private funds" (those with assets under management of between $25 million and $100 million, as more fully described in the next paragraph) to determine whether the funds pose a systemic risk, and to provide for the registration and examination procedures necessary in light of any such risk.

Furthermore, Section 410 of the PFIARA amends Section 203A(a) of the Investment Advisers Act to effectively define "mid-sized" investment advisers and to alter the relationship between federal and state regulation of these advisers. Section 410 expands the existing federal prohibition from federal registration for an adviser to non-registered investment companies registered with the state where it maintains its principal office if it has assets under management of less than $25 million. Mid-sized investment advisers, or those advising non-registered funds with aggregate assets between $25 million and $100 million, and which are registered at the state level, are now also prohibited from registering federally unless they are advising a federally registered investment company or business development company. Federal registration is permitted if the adviser would be required under this provision to register with at least 15 states. Applicable regulations have been amended to clarify and expand on these provisions, and to provide transition rules for those switching from state to federal registration and vice versa. This *de facto* delegation of authority to states is expected to result in some advisers withdrawing their registration with the SEC and registering at the state level instead.[4]

But the most significant change for advisers to private funds should be emphasized: As a result of the PFIARA, many advisers to private funds are now subject to the reporting, recordkeeping, compensation and other rules applicable to registered investment advisers. A discussion of the initial new reporting requirements follows.

Private Fund Reporting Specifics

Significantly, Section 404 of the PFIARA amends 204(b) of the Investment Advisers Act to require that private fund advisers maintain records and file reports as the SEC deems necessary and appropriate in the public interest and for the protection of investors, or for the assessment and monitoring of systemic risk by the Financial Stability Oversight Council (FSOC) created by the Dodd-Frank Act. Section 404 contemplates that any records and reports would include, for each private fund, information regarding the amount of assets under management and the use of leverage (including off balance sheet leverage), counterparty credit risk exposure, trading and investment positions, valuation policies and practices of the fund, types of assets held, any side arrangements giving some investors more favorable treatment than others, trading practices and such other information as the SEC and the FSOC determine are necessary and appropriate. And a confidentiality provision of the Investment Advisers Act, stating that the SEC is not authorized to require public disclosure of information with respect to clients of the investment adviser, has been amended to allow the SEC to require disclosure for purposes of assessment of potential systemic risk, as well as in an enforcement-related proceeding.[5]

Form ADV

Accordingly, Rule 203-1 under the Investment Advisers Act, which provides for application for investment adviser registration on Form ADV, was revised in June 2011 to state that investment advisers previously exempt under Section 203(b)(3) of the Investment Adviser Act were required to register as investment advisers by March 30, 2012. In addition, new Rule 204-4[6] provides that investment advisers relying on exemptions under

Sections 203(l) or (m) of the Investment Advisers Act, regarding venture capital fund advisers and private fund advisers respectively, must also complete and file reports on Form ADV but provide only the information required of exempt reporting advisers on that form and not the firm brochure, brochure supplements or related information set forth in Part 2 of the form. Form ADV is a publicly available document.

In summary, Form ADV requires basic identification information for the firm and its management, as well as information regarding the amounts under management; the number and types of clients advised; compensation arrangements; advisory and other business activities; other general practices and any prior criminal, civil or regulatory proceedings. Form ADV is to be filed electronically with the Investment Adviser Registration Depository (ARD), and there is a filing fee. The SEC advises that Form AVD applications typically take 45 days to process and approve. Temporary hardship exemptions, allowing filing of Form ADV by paper and following up with electronic filing, are available. The form must be amended annually, or more frequently if required under the instructions to the form.[7] A final report for exempt reporting advisers must be filed when the adviser ceases to perform the role, the adviser no longer meets the definition of exempt reporting adviser or the adviser applies for registration. Furthermore, Rule 204-2 under the Investment Advisers Act has been revised to require additional recordkeeping for all investment advisers, and to provide transition rules for advisers newly registered pursuant to the PFIARA.

Form PF

In SEC Release No. IA 3308, issued Oct. 31, 2011, the SEC added Rule 204(b)-1 under the Investment Advisers Act, initially proposed earlier in the year,[8] requiring registered investment advisers to one or more private funds and who have at least $150 million in private fund assets under management to report information for use by the FSOC in monitoring systemic risk in U.S. financial markets, as contemplated under Sections 404 and 406 of the PFIARA. This rule requires the filing of the newly created Form PF. Like the Form ADV, this form is to be filed electronically, along with a filing fee. Amendments are required at least annually, when amendment to Form ADV is required, and more frequently as described below. A temporary hardship exemption permitting paper filing is available.

The form itself requires information regarding the funds advised, their assets, borrowings, investments, strategy and performance, as well as information regarding counterparties, liquidity, financing and investors. The scope of information required, and the frequency of filing, varies with the type of fund and the aggregate amount of assets under management.

The large majority of private fund advisers required to file Form PF will only need to complete Section 1, which requests basic information regarding all private funds advised, as well as the funds' assets under management, performance and use of leverage. Larger private fund advisers, including advisers having at least $1.5 billion in assets under management attributable to hedge funds, $1 billion in assets under management attributable to liquidity funds or registered money market funds, or at least $2 billion in assets under management attributable to private equity funds, are required to complete additional sections of Form PF.[9] Large hedge fund advisers must complete Section 2 of Form PF, large liquidity fund advisers Section 3 of the form, and large private equity fund advisers Section 4 of the form. Although relatively small in number, these advisers are estimated by the SEC to manage a large majority (approximately 75 to 80 percent) of the funds invested in this market.

Each of the additional sections of Form PF requires more specific information designed to monitor and identify potential items and trends of systemic risk for those particular types of funds. Section 2, for large hedge funds, includes questions regarding exposure by asset class, geographical concentration and turnover, as well as certain information relating to fund exposures, leverage, risk profile and liquidity. Reporting of position-level information is not required. Large liquidity funds are required in Section 3 to provide information on their portfolios and risk profile, and state whether the fund complies with Rule 2a-7 under the Investment Company Act regulating registered money market funds. The questions for large private equity fund advisers in Section 4 concern the extent of leverage in the funds advised, the use of bridge financing, and the investments in financial institutions by the funds advised.

As per the Form PF instructions and the issuing release, large private equity advisers and all smaller private fund advisers must file Form PF once per fiscal year; the filing is due 120 days from the end of the relevant fiscal year. Large hedge fund advisers and large liquidity fund advisers must make filings each fiscal quarter, with large hedge fund advisers having to file within 60 days of the end of the quarter and large liquidity fund advisers within 15 days from quarter end. The initial compliance date for Form PF reporting was June 15, 2012, for: 1) advisers having at least $5 billion in assets under management attributable to hedge funds, or to liquidity funds and registered money market funds, as of the last day of the fiscal quarter recently completed prior to June 15, 2012, or 2) advisers having at least $5 billion in assets under management attributable to private equity funds as of the last day of its first fiscal year to end on or after June 15, 2012. The compliance date for other advisers subject to the rule is Dec. 31, 2012.

For advisers to all types of funds, a final report is required to indicate that an adviser is no longer required to file Form PF. Failure to file reports can lead to revocation of investor adviser status.

An adviser's filed Form PF will not be available publicly. The SEC has indicated its understanding of the confidential nature of the information to be provided by fund managers. Nevertheless, there are concerns that in an age of Wikileaks an unauthorized disclosure is possible.

Other Changes of Interest

Among the many recently enacted changes to the law, there are several other issues of possible interest to private funds and their advisers. A brief description of each follows.

Rule 206(4)-5 under the Investment Advisers Act has been revised to include "exempt reporting advisers" (advisers to venture capital and small private funds) in the prohibition from providing advisory services to a government entity within two years after making a political contribution to an officer of that public entity.

The SEC has jointly published, along with the Treasury Department, Federal Deposit Insurance Corporation (FDIC) and the Federal Reserve, proposed rules prohibiting and restricting the ability of certain banking and financial institutions to engage in proprietary trading or to have certain interests in and relationships with hedge or private equity funds.[10]

And finally, Section 416 of the PFIARA directs the comptroller general to conduct a feasibility study with respect to the formation of a self-regulatory organization (SRO) to oversee private funds, roughly analogous to the Financial Industry Regulatory Authority (FINRA) for broker-dealers. A report issued by the General Accounting Office (GAO) in July 2011, in accordance with the PFIARA's directive, found that forming such an SRO would be feasible, but would require significant work and funding to establish. The report also opined that such an SRO would benefit from the resources and expertise available outside of the SEC, and that the SRO may serve to lighten the SEC's burden in this area and free up government resources. The GAO noted, however, that establishing the SRO might risk creating a "fragmented" regulatory environment, with possibly overlapping regulatory schemes and gaps in regulation.

Conclusion

In public statements, the SEC has indicated that it expects to monitor the implementation of the regulations and take note of any issues that develop, all with an eye toward adjusting and fine-tuning reporting requirements in order to respond to any such issues. Nevertheless, it is clear that a regulatory atmosphere of increased monitoring and scrutiny is here. And the possibility of further substantive laws, rules or other prohibitions based on the information the FSOC has received and its interpretation of the data is very real. ■

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Endnotes

1. Qualified purchasers are defined to include individuals or entities owning at least $5 million in investments, or persons acting for their own account or the accounts of other qualified purchasers who in the aggregate own and invest, on a discretionary basis, at least $25 million in investments. Investment Company Act Section 2(a)(51).
2. Rule 202(a)(11)(G)-1 under the Investment Advisers Act, adopted in SEC Release No. IA-3220 in June 2011, sets forth detailed rules regarding family offices.
3. Unless otherwise specified, all references to SEC Rules are to rules under the Investment Advisers Act.
4. In addition, the exemption from the prohibition on registration for "pension consultants" is amended to include only those advisory plans with an aggregate value of at least $200 million, as opposed to the prior threshold of $50 million, again meaning that fewer of such advisers need to register with the SEC. Regulations have been revised to facilitate the registration of ratings agencies at the state rather than the federal level as well. *See* Rule 203A-2 and Release No. IA-3221.
5. Section 405 of the PFIARA.
6. Added in Release No. IA-3221 in June 2011.
7. Rule 204-1.
8. The initial proposal is contained in Release No. IA-3145, issued in Jan. 2011. The final regulation has been scaled back in several respects from the original proposal, with higher dollar amount thresholds and later filing deadlines, among other things.
9. Hedge fund is defined in Form PF generally to include any private fund having any of the following three characteristics, (a) a performance fee calculated using account market value (rather than merely realized gains) as a factor, (b) high leverage or (c) short selling. Liquidity fund is defined as a private fund that seeks to generate income by investing in a portfolio of short term obligations, with the goal of maintaining a stable net asset value per unit or minimizing principal liability for the fund's investors. Private equity fund is defined as any private fund that is not a hedge fund, liquidity fund, real estate fund, securitized asset fund or venture capital fund and whose investors do not have redemption rights in the ordinary course.
10. Release Nos. 33-65545 and 34-66057.

Commentary

Women in the Boardroom

by Veronica Montagna

Early this spring, as predictably as the crocus spring from the earth, the proxy statements of thousands of companies whose stock is publicly traded in the United States will be delivered to their stockholders. These proxy statements will contain the names and faces of the company's nominees for election to its board of directors. Predictably, the nominees will be well-qualified, well-respected captains of industry, as they should be since they represent the pinnacle of power in business, and the proxy statements will include biographies that herald the nominees' achievements. The nominees frequently are the chief executives or hold other senior positions in public companies. They lend their prestige to a company's board and evoke confidence among its stockholders. With limited exceptions, these director candidates tend to be the same nominees who are re-elected year after year. Just as predictably, these nominees will be almost uniformly male, despite overwhelming evidence that establishes the multiple positive effects that occur when women take a seat in the boardroom.

The fact that the under-representation of women in the boardroom has not yet become *the* hot button corporate governance issue for activist shareholders is simply inexplicable. Institutional investors, activist groups and influential proxy advisory firms must become more vocal in their criticism of companies that fail to address the issue of gender diversity in the boardroom. The simple truth is that it should no longer be tolerated when a publicly traded company in the United States does not have a significant numbers of women on its board of directors.

The statistics here in the United States, as well as abroad, demonstrate that there has been little headway made toward increasing the numbers of women serving on company boards. Catalyst Inc., a nonprofit organization that serves as a resource for research, information and advice about women in the workforce, recently conducted a census to examine the representation of women on the boards of Fortune 500 companies. The Catalyst census revealed that, in 2011, women held 16.1 percent of the board seats at Fortune 500 companies.[1]

Governance Metrics International (GMI), an organization that conducts research and analysis of risks affecting the performance of public companies worldwide, also studied the composition of U.S. public company boards. Among the 1,756 U.S. public companies involved in the GMI Ratings Survey, the percentage of women directors on these boards increased only marginally to 12.6 percent, up just .5 percent from 2009 to 2011.[2] According to the GMI Ratings Survey, over 70 percent of U.S. boards had at least one female director, but only 10 percent had three or more women directors and just two percent of board chairs were women. The GMI Ratings Survey examined data on over 4,300 companies in 45 countries and found that among industrialized nations, including Australia, Hong Kong, Japan, Singapore, Austria, Belgium, France, Germany, Greece, Italy, Netherlands, Spain, Switzerland, the United Kingdom, Denmark, Finland, Norway, Sweden, Canada and the United States:

- 11.1 percent of directors were women,
- 63.3 percent of companies had at least one woman on the board, and
- 10.5 percent of companies had three or more female directors.

Among emerging nations, including Brazil, Mexico, China, India, Indonesia, Malaysia, South Korea, Taiwan, Russia and South Africa, the statistics were, as expected, more problematic:

- 7.2 percent of directors were women,
- 44.3 percent of companies had at least one woman on the board, and
- 6.3 percent of companies had at least three female directors.

The statistics and the studies that demonstrate the positive impact of female directors are clearly not in sync and progress has been painfully slow. The problem of under-representation of women in public company boardrooms is in some respects a lack of supply. The executives that rise to the top of the corporate executive pipeline are traditionally the preferred candidates when board candidate searches are conducted, and few women rise to the top of the corporate executive pipeline.

The Benefits of Remedying the Under-Representation of Women on Boards, Including Why Three or More Women is a Critical Mass

The board of directors owes a duty to act in the best interests of all stockholders of the company, male and female, and should not be homogenous. Like society, a board should have many voices, be of many colors and include significant numbers of women. Since women comprise greater than 50 percent of the global workforce and the consuming public, and own and manage significant wealth, including stock investments in public companies, a simple argument could be made that a gender-balanced board more closely resembles the constituency the board has a duty to serve.

When Facebook announced its initial public offering in Feb. 2012, its seven-member board was entirely male. California State Teachers Retirement System (CalSTRS), the largest public pension fund for public school teachers in the United States and a Facebook investor, wrote a letter to Facebook's chairman and chief executive officer, Mark Zuckerberg, to express its disappointment that the Facebook board would not include any women members, which it considered a "glaring" omission. CalSTRS strongly urged Zuckerberg to include women on the Facebook board, indicating that when the company's mission and subscriber base are considered it made "good business sense." Facebook was publicly chastised by activist groups like 2020 Women on Boards, a nonprofit company that has as its objective ensuring that 20 percent of all directors are women by 2020, and Women Corporate Directors, an organization that promotes female board membership as well. Said Susan Stautberg, a founder of Women Corporate Directors: "It doesn't make sense for a company that claims to be so forward looking to not have any women directors. If they just have an old boy's network in their boardroom, they won't have access to diverse ideas and strategies."[3]

Anne Mulcahy, the former CEO and chairman of Xerox Corp. and herself a director on several public boards, commented: "We're long past having to defend or explain why women should be on boards, given all the data that shows how companies with female directors perform better…It's unfortunate when companies with a large percentage of women constituents don't reflect that in their boardrooms."[4]

Four months after completing its initial public offering, Facebook announced the appointment of its chief operating officer, Sheryl Sandberg, to the Facebook board.

As Anne Mulcahy indicated, there is a strong business argument for increasing the numbers of women in the boardroom. Research shows that companies with greater numbers of women participating in boardroom deliberations financially outperformed companies with the lowest percentages of women directors by significant margins. A 2012 Credit Suisse Research Institute study examined the performance of 2,360 public companies worldwide with a market capitalization of more than $10 billion. The researchers found that the presence of even one female board member resulted in outperformance of comparable companies with all-male boards by 26 percent over a period of six years, and that the benefits associated with women directors was most pronounced after the 2008 economic downturn.[5] The companies with female directors tended to have less debt and were more conservative in their approach to corporate risk-taking, key predictors of financial outperformance in the post-2008 period. Other studies found the same correlation exists between the percentage of women senior executives and financial performance.[6]

Among its primary responsibilities, a board of directors selects the chief executive officer and other members of the senior management team, and ensures that a succession plan exists for the management team. Research conducted by Catalyst analyzed the relationship between the percentage of women directors on the boards of 359 Fortune 500 companies in 2001 and the percentage of women senior executives at the same companies five years later. The research revealed that the number of female directors on a board was predictive of the number of female senior executives of the company in the future. The more seats on the board that were held by women meant the more female senior executives the company would have in the future.

Significantly, the women directors had the greatest impact on the number of women in line for business positions (profit-making activities like manufacturing, production, marketing and sales) as opposed to cost center positions (functions such as human resources, legal, finance and public relations, that support business operations). This finding is important because line experience is often viewed as a requirement for advancement to chief executive officer and other top leadership roles.[7]

The researchers offered several explanations for why the number of women directors was a strong predictor for greater numbers of women advancing into upper management. First, companies with female directors are more likely to have policies and programs designed to propel female employees into leadership roles. Second, women directors serve as role models to female employees in the executive management pipeline. Third, a company able to point to a gender-diverse board and a gender-diverse management team is more attractive to the brightest young women who are seeking the best places to work.

In 2010, the British government undertook a study of the issue of women in the boardroom.[8] Like the United States studies, the British study found a strong connection between a company's operational and share price performance and higher proportions of women directors. In addition, the British study indicated that women directors took their directorships more seriously, prepared more thoroughly for board meetings and were more likely to ask pointed questions during board deliberations. The companies with gender-diverse boards were found to be more likely to pay attention to and control risk and had a reduced chance of corporate insolvency. These companies were more likely to focus on non-performance measures like employee and customer satisfaction, diversity and corporate social responsibility, and to have new director education programs and closely monitor board performance. The British study found that the failure of companies to maximize the talents of women in the boardroom was shortsighted at best, since female directors were more inclined to understand the needs and desires of female customers.

A research project conducted through the Wellesley Centers for Women examined the impact of women directors on the corporate governance of Fortune 1,000 companies and found that women directors adopt a collaborative leadership style that enhances listening to opposing views and broadens the discussion to include the viewpoints of multiple parties.[9] The Wellesley study also identified the importance of a critical mass of women on a board. While the Wellesley study revealed that a single woman director may positively impact board function, these solitary women reported (or males on the board observed) that they were not listened to or were excluded from certain activities and decision-making, were made to feel that their views represented a "women's point of view" and were sometimes the target of inappropriate behavior that indicated male directors noticed their gender more than their individual contributions to the board.[10]

The personal experiences of Brooksley Born, who served as the chair of the Commodity Futures Trading Commission from 1996 to 1999, demonstrate the challenge of being the only woman in the room. During her tenure at the government agency, she was deeply worried about the risks of over-the-counter derivatives and, in numerous congressional hearings, strongly urged for regulation of the derivatives. But the U.S. economy was humming along at the time and her warnings were entirely ignored. A decade later, the same investment vehicles Brooksley Born warned of would contribute to the collapse of financial markets. A *Washington Post* article heralding Born as "the woman who predicted the 2008 financial crisis" cited news reports during the time Born spoke out about the risks of over-the-counter derivatives summing up reaction to Born's warnings as being, "The nation's top financial regulators wish Brooksley Born would just shut up," and Born is "a salmon swimming against raging currents."[11]

The Wellesley study concluded that three women directors constitutes a critical mass, after which the board dynamic changes and the benefits associated with women on the board are more likely to occur. On boards with three or more women, the women were perceived by the other directors as individuals with different personalities, strengths and convictions, each having their own views on the matter at hand. They were more likely to influence the outcome of the boardroom discussions. Corporate governance improved because the women directors were more persistent than their male counterparts, required direct and detailed answers and, as a consequence, difficult issues were more likely to be spotted and addressed. Such boards were more likely to consider the concerns of not only the company's stockholders, but its employees, customers, suppliers and the community at large, and to take a collaborative approach to decision-making. The Wellesley study concluded that gender diversity was so beneficial that when filling board vacancies, board nominating committees should *not* strive to be gender-blind in considering board candidates.

Various Approaches to Achieving Board Gender Diversity

In the face of all of this evidence, what is being done and what else can and should be done to improve board gender diversity? The GMI Ratings Survey revealed that among the studied countries a wide range of approaches are being used to try to improve board gender diversity. These measures include legislation that imposes quotas on the numbers of women on boards, corporate governance guidelines and listing exchange standards, mentoring programs and other voluntary initiatives. The wide range of initiatives has produced a wide range of results among nations. Certain European nations are now well ahead of the United States in terms of achieving gender diversity in the boardroom. On the other hand, some countries are doing very little. In Japan, for example, women occupy an abysmal one percent of all board seats.[12]

Legislative Action by European Nations

Many European nations have enacted legislation that imposes gender quotas for company boards. These countries are led by Norway, which, in 2006, enacted a law that required that its public companies have boards comprised of 40 percent women by 2008 or face fines. Norway now has the greatest percentage of female directors of any country, currently 36.3 percent, and almost 61 percent of Norwegian companies have at least three women on their boards, according to the GMI Ratings Survey.[13]

Other nations in Europe have followed Norway's lead. Spain enacted a law in 2007 that requires public companies to have boards comprised of 40 percent women by 2015. Non-compliant Spanish companies will not be penalized, but the companies that reach the quota will be rewarded with priority status in the allocation of government contracts.[14] In 2010, France's government enacted legislation that requires French boards to be 20 percent female by 2013 and 40 percent female by 2016.[15] Non-compliance will render all board nominations void and prohibit a company from paying director fees to its board members.[16] The percentage of female directors in France is currently near 17 percent, and nearly a third of French companies have at least three female directors. In Sept. 2012, the upper house (the Bundesrat) of Germany's Parliament introduced a proposed rule that will require German companies to reserve for women at least 40 percent of the seats on their supervisory boards. The rule includes a phase-in period that requires 20 percent of board seats to be held by women by 2018 and the full 40 percent must be achieved by 2023. The lower house (the Bundestag) of Germany's Parliament is tasked with drafting the legislation.[17]

In addition, based on recent actions of the European Commission, much of the rest of Europe will soon be under a quota system that will affect a uniform approach to the issue in European Union nations. In March 2011, the European Union commissioner for justice and fundamental rights, Viviane Reding, met with the chief executives and chairs of publicly listed European companies to discuss the under-representation of women on their boards. Commissioner Reding challenged the leaders of these companies to sign a pledge to increase the numbers of women on their boards to 30 percent by 2015, and to 40 percent by 2020. Only 24 companies had signed the pledge a year after its introduction. The European Commission, finding no tangible results from the voluntary program, estimated that it would take more than 40 years to attain gender balance (40 percent women) in the boardroom at the current rate of improvement.[18] After a public comment period, on Nov. 14, 2012, the European Commission announced a directive[19] to each member nation to require that its public companies with more than 250 employees or more than 5,000,000 in revenue boost the number of women filling non-executive seats on their boards to 40 percent by 2020, and to report each year on the composition of their boards. European Union member states will be required to impose sanctions on companies that fail to meet the quotas. Said Commissioner Reding, "I am not a great fan of quotas; however, I like the results they bring."

Listing Standards

Commencing with fiscal years ending on or after Dec. 31, 2011, companies that are listed on the Australian Securities Exchange must report on their diversity policies and specific objectives for improving gender diversity. This listing requirement, as well as a mentoring program conducted by the Australian Institute for Company Directors, which matches long-serving directors with professional women, have been credited with a 5.4 percentage point increase, to 13.8 percent, in the number of females serving on the boards of Australian companies.[20] The United Kingdom has declined to follow the European trend toward government intervention. Based on recommendations contained in the British study, starting in Oct. 2012, the London Stock Exchange requires that each listed company disclose its policy and objectives with regard to board diversity, disclose annually the progress made toward achievement of its objectives and consider board diversity as a factor in evaluating the effectiveness of the board.[21]

The United States Proxy Solicitation Rules and the Dodd-Frank Act

In the United States, there are no listing rules or legislation that mandate that companies achieve board gender diversity. The proxy solicitation rules of the Securities and Exchange Commission (SEC) require that public companies disclose in their proxy statements how they identify board candidates, the minimum qualifications required to serve as a director and the qualities and skills considered important for candidates to possess. A company must disclose how its nominating committee identifies and evaluates director nominees, and whether, and if so how, it considers diversity.

Gender diversity is not specifically addressed in the proxy rules. If a company has a diversity policy for identifying director nominees, it must describe how the diversity policy is implemented and how the nominating committee evaluates its effectiveness.[22] A company that publicly discloses that it has a diversity policy, but nonetheless nominates an all-white male slate of candidates year after year could eventually find itself in the uncomfortable position of having to explain the purpose of a diversity policy it does not follow. The SEC staff could determine to issue a comment letter to the company on the issue, resulting in more embarrassing disclosure.

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, which became law on July 21, 2010, directed the SEC to establish an Office of Minority and Women Inclusion (OMWI) to be responsible for "all matters of the agency relating to diversity in management, employment and business activities."[23] Among the OMWI's duties is to assess the diversity policies and practices of entities regulated by the SEC.[24] The OMWI must submit an annual report to Congress that contains information related to the government's hiring of minority-owned and women-owned businesses, as well as "any other information, findings, conclusions and recommendations for legislative or agency action, as the OMWI director determines appropriate."[25] To date, the OMWI has not made any public recommendations or assessments on the issue of diversity. The OMWI's first annual report to Congress simply indicated that it has held discussions with business leaders with the aim of developing standards to assess diversity policies and practices of regulated entities.[26]

The Role of Nominating Committees and Other Parties

A company truly committed to increasing the ranks of women serving on its board must, when conducting a search for board candidates, look beyond the traditional candidate, the chief executive officer, and further into the ranks of senior management to find women, since chief executive officers tend to be white males. A nominating company must think outside the box and consider candidates from outside the corporate setting, such as women entrepreneurs, academics, consultants, lawyers, doctors and executives from nonprofit organizations. The nominating committee should not be gender blind. It should perceive its role in increasing the number of female director candidates as among its most important duties and should insist that any search firms engaged to identify board candidates always include qualified women in the slate of candidates.

One of the criticisms of nominating committees is that once a director is elected to the board he seems to have achieved tenure and will be re-nominated and reelected year after year. This has the effect of limiting the opportunities for qualified women to serve on a board. A nominating committee should weigh each director's contributions to the board, including board attendance, preparedness and participation, and decline to re-nominate ineffective directors. A company should also consider limiting the number of consecutive years a director is permitted to serve on the board.

Shareholders, particularly institutional shareholders controlling large blocks of voting stock, have the power to grab the attention of companies that have ignored the issue of board gender diversity by withholding votes in the election of directors. A shareholder could also use the shareholder proposal process to force a company to respond to the issue. There are also investment management companies that cater to investors who desire to invest in the stock of socially responsible companies. These investment management firms will consider a company's board diversity policies in determining whether to invest client funds in the company's stock. The influential proxy advisory services, Institutional

Shareholder Services Inc. and Glass, Lewis & Co., LLC, have the ability to place a spotlight on the issue by recommending shareholders vote against any slate of directors that does not include women.

Many nonprofit organizations are available to help place qualified women with companies seeking female director candidates. In addition to 2020 Women on Boards, the nonprofit company that took Facebook to task for its lack of female directors, these organizations include:

- the DirectWomen Board Institute, a program that identifies and promotes qualified women lawyers to serve on the corporate boards of public companies. Approximately 20 female attorneys are selected to attend DirectWomen's Board Institute, an annual two-day program that provides orientation and updates women on key issues related to serving as directors to prepare them to join the boards of major United States companies. DirectWomen's website indicates that persons desiring to receive notification when the application for Direct Women's 2013 Board Institute become available should send an email to sgevlin@directwomen.org with name and contact information;
- Diverse Director Datasource (www.gmi3d.com), owned and operated by GMI as a clearinghouse for the registration of potential corporate director candidates with a special emphasis on a more diverse range of backgrounds, perspectives, skills and experience; and
- The Thirty Percent Coalition (www.30percentcoalition.org), a coalition of senior executives, national women's organizations, institutional investors, corporate governance experts and board members committed to collaborating to achieve gender diverse public company boards. The organization's goal is at least 30 percent female representation on public company boards by the end of 2015.

Conclusion

Every public company in the United States and elsewhere should strive toward achieving a critical mass of women directors on its board. Companies that have one or two women on their boards already should not be complacent. Companies without women on their boards should take strident action to remedy the situation before their next solicitation of proxies in the election of directors. The research overwhelmingly supports that bringing more women into the boardroom is a win-win situation for all involved. Women directors bring to the board a new perspective and deliberation style that enhances the quality of boardroom discussions, reduces corporate risk and improves performance. A board that includes a critical mass of women will be well equipped to make decisions based on thoughtful collaboration of a group of individuals with diverse backgrounds, experiences and perspectives.

The European approach to the under-representation of women on boards has now solidified around quotas. As European companies rush to increase the numbers of women serving on their boards in order to meet the compliance deadlines, the spotlight will fall on the United States. Public companies in the United States, the SEC and Congress will come under increasing pressure from shareholders and activist groups who will call for actions to keep pace with the progress in European companies. However, a solution involving a quota system is unlikely in the United States. What is certain is that the success of any plan to achieve gender diversity in the boardrooms of public companies in the United States will necessarily involve the commitment of the companies and their officers and directors, stockholders and executive search firms, among others, in addition to a supporting role from government.

Veronica Montagna is an associate at McCarter & English, LLP, who counsels companies on compliance and reporting obligations under federal and state securities laws and best practices and emerging trends in corporate governance and also represents clients in mergers and acquisitions, dispositions of business assets and secured and unsecured loan transactions. She has three young daughters for whom she hopes the doors to the public company boardroom will be wide open. This article was originally written for and appeared in the Dec. 2012 edition of Women in the kNOW, a newsletter published by the Women's Initiative of the law firm of McCarter & English, LLP.

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23. Section 342 of the Dodd-Frank Act, Pub. Law 111-203, H.R. 4173
24. *Id.* at Section 342(b)(2)(C).
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Business Law Student Writing Competition

by Gianfranco A. Pietrafesa

The Business Law Section recently sponsored a writing competition for law students interested in business law. It was my hope that the competition would attract law students interested in business law to join the section as young lawyers.

The winning entries were written by **Yasmine N. Fulena**, a second-year student at Seton Hall, and **John Shindle**, a third-year student at Rutgers-Camden. Congratulations on a job well done! Their memoranda are published in this newsletter.

The competition was open to students who were entering their second or third year at Seton Hall Law, Rutgers Law-Newark and Rutgers Law-Camden. Students were required to write a memorandum based on a hypothetical fact pattern and the three court opinions provided to them. No research was required or permitted; instead, the competition was based on an analysis of the law, the application of the law to the facts and the preparation of a memorandum. We received nine entries from Seton Hall and five from Rutgers-Camden.

The hypothetical fact pattern involved a transaction structured as an asset purchase and the issue was whether two contracts could be assigned from seller to buyer in such a transaction. The fact pattern was based on a typical assignment that a young business lawyer would receive when working on an M&A transaction and involved an analysis of contract law, which was a course that the students would have taken prior to participating in the competition. The assignment memorandum from partner to associate (*i.e.*, law student) setting forth the fact pattern is published in this newsletter.

The volunteer attorneys reviewing the memoranda did so without knowing the identifies of the students. Each memorandum was reviewed by three judges. They graded the students' memoranda based on writing quality, analysis and legal reasoning, and compliance with competition rules, using the following factors:

1. The memorandum reflects a sound analysis and the correct result on the assignment of the lease agreement;
2. The memorandum reflects a sound analysis and the correct result for the assignment of the trademark license agreement;
3. The memorandum uses proper Bluebook citation;
4. The memorandum is well organized, uses headings effectively, etc.;
5. The quality of the writing (*i.e.*, is the memorandum easy to read and understand); and
6. The memorandum offers a practical suggestion/conclusion.

The winning entries were written by Yasmine N. Fulena, a second-year student at Seton Hall, and John Shindle, a third-year student at Rutgers-Camden. Congratulations on a job well done! Their memoranda are published in this newsletter.

In addition to having their memoranda published in the newsletter, the winning law students will be joining the section's board of directors at a dinner meeting. They will also receive three books that they can use when they enter private practice: Stuart L. Pachman's *Title 14A – Corporations* (donated by Gann Law Books), Clark E. Alpert's *Guide to New Jersey Contract Law* (donated by NJICLE), and Paul A Rowe's *New Jersey Business Litigation* (donated by New Jersey Law Journal Books).

Go to Index

A lot of time and effort went into the competition. I feel it was well worth it to attract students and young lawyers to the section and get them to appreciate the value of section membership and active participation in section committees, seminars and other events. The competition would not be possible without the support of many people, and I want to take this opportunity to publicly thank them.

I want to thank the directors and members of the section who volunteered to judge the memoranda: Orville R. Cockings, Colleen R. Donovan, Robert J. Feinberg, W. Raymond Felton, Barry Gartenberg, Laura Magedoff, Lori I. Mayer, Veronica Montagna, Sheila O'Halloran, William Skinner, Alan Walter and Seth Zuckerman. I also want to thank the other section members who volunteered to help. Hopefully the competition will grow next year and we will need more judges.

I also want to thank the deans of the three law schools for participating in the competition, as well as the other deans and professors at the law schools for their valuable assistance: Dean Rayman L. Solomon of Rutgers-Camden, Dean Patrick E. Hobbs of Seton Hall, Dean John Farmer of Rutgers-Newark, Professor Arthur Laby of Rutgers-Camden, and Dean of Students Cara Herrick Foerst of Seton Hall.

Finally, I want to thank Michael Protzel, publisher of Gann Law Books; Robert Steinbaum, publisher of the *New Jersey Law Journal*; and Angela C. Scheck, executive director of the New Jersey State Bar Association, for their generous donations of the books awarded to the winning students.

If I inadvertently forgot to thank someone, please accept my apologies. In conclusion, if section members want to get involved in the 2013 business law student writing competition, please feel free to contact me at gpietrafesa@archerlaw.com.

Gianfranco A. Pietrafesa is a partner in Archer & Greiner, in its Hackensack office. He is the immediate past chairman of the Business Law Section.

New Jersey State Bar Association
Business Law Section
Business Law Student Writing Competition

Eligibility: Any person who in Sept, 2012 is enrolled as a second or third year student at Seton Hall University School of Law, Rutgers School of Law-Newark or Rutgers School of Law-Camden, and interested in business law, is eligible to enter the writing competition.

Submission Information: The student must read the attached memorandum with hypothetical facts about a pending business transaction and the three attached cases (*Owen v. CNA Ins.*, 167 N.J. 450 (2001); *Garden State Buildings v. First Fidelity Bank*, 305 N.J. Super. 510 (App. Div. 1997); and *Bel-Ray Co. v. Chemrite*, 181 F. 3d 435 (3d Cir. 1999)) and prepare a legal memorandum with his or her analysis and conclusions. Submissions must be sent by email to BLSWritingCompetition@gmail.com by Sept. 30, 2012, at 5 p.m. EST. Submissions must not exceed 2,500 words in length (or a maximum of 8 pages) on 8.5 x 11-inch pages, with one inch margins, double-spaced using 12-point Times New Roman font (10-point font for any endnotes) with Bluebook format for citations. Submissions must be made by email attachment in Microsoft Word format, with the cover page as a separate attachment.

For anonymous evaluation of the entries, no information that could identify the author should appear anywhere in the memorandum. Each entry must have a separate cover page (not included in the 2,500-word limit) that includes the following contact information: (1) student name; (2) address; (3) phone number; (4) email address; (5) law school; and (6) year in law school. The memorandum must be the original work of the individual student submitting the entry, and must not have been previously published.

Judging: The panel of judges will consist of a committee of members of the board of directors of the Business Law Section and other volunteer business lawyers, who will judge the papers without knowledge of the student's name. Papers will be judged by the following criteria: (1) writing quality; (2) analysis and legal reasoning; and (3) compliance with the competition rules.

Awards: Winning entries will be announced and winners notified no later than Nov. 30, 2012. One winning paper will be selected from each law school. Winning students will have their papers published in the March 2013 Newsletter of the Business Law Section (distributed to the 1,000+ members of the Section). Winning students will also be invited to attend a dinner meeting of the board of directors of the Business Law Section and will receive a copy of *Title 14A – Corporations* (donated by Gann Law Books), *Guide to New Jersey Contract Law* (donated by NJICLE), and *New Jersey Business Litigation* (donated by New Jersey Law Journal Books).

Memorandum

To: Partner

From: Yasmine Fulena, Newark, NJ,
Seton Hall Law, Class of 2014

Issue

Whether there will be any consequences if Sam's, Inc. (Sam's) assigns its lease agreement with its landlord and its trademark license agreement with Orange, Inc. (Orange) to Baker, LLC (Baker), without obtaining the required prior written consent from its landlord and Orange, where an assignment clause is enforced if it contains express provisions that any assignment shall be void if not made in certain specified way, absent which the assignment is still effective but the obligor retains the right to damages for breach of terms forbidding assignment, and where the lease assignment clause states that the lease "may not be assigned or subleased by Tenant without prior written consent of the Landlord", while the trademark license assignment clause states that "any assignment or delegation in violation of this provision shall be null and void."

Brief Answer

If the assignment provision of a contract contains language restricting only the parties' right to assign, then the clause is treated as a covenant not to assign, an assignment is valid although done in violation of the clause, and the non-assigning party can claim damages from the assigning party for breach of terms forbidding the assignment. If the assignment clause contains express provisions that restrict the parties' power to assign, then the non-assigning party has the right to invalidate an assignment done contrary to the terms, unless it clearly waives this right. Therefore, if Sam's does not obtain prior written consent from its landlord before assigning the lease agreement to Baker, the likely consequence is that a court will find the assignment is valid because the language in the assignment clause only limits the parties' right to assign. However, the landlord can claim damages from Sam's for breach of a contractual term. If Sam's assigns its agreement with Orange to Baker without obtaining prior written consent from Orange, the likely consequence is that a court will enforce the assignment clause because it expressly restricts the parties' power to assign ("any assignment done without the prior written consent of the other party will be null and void"), and the assignment will be void, unless Orange chooses to waive its right to void the assignment.

Statement of Facts

Our client, Baker, is buying Sam's business. This transaction is structured as an asset purchase. Consequently, Sam's contracts will have to be assigned to Baker. Two of Sam's numerous contracts are of utmost importance to Baker: Sam's lease agreement with its landlord for its building in Hackensack, and Sam's trademark license agreement with Orange.

Sam's building in Hackensack houses a light manufacturing plant and warehouse. The company has a long-term lease with the landlord below market rents. Sam's informed our client that the landlord has complained about the rent for the last couple of years. The assignment clause in the lease provision states: "This Lease Agreement may not be assigned or subleased by Tenant without prior written consent of Landlord." Sam's license with Orange allows Sam's to manufacture and sell various products bearing Orange's name. This particular agreement generates 70% of Sam's revenue. Sam's also informed Baker that Orange only entered into this trademark license after carefully evaluating Sam's capabilities. The assignment provision for this lease reads "Neither party may assign this Agreement, nor assign any of its rights or delegate any of its obligations hereunder, without the prior written consent of the other party. Any purported assignment or delegation in violation of this provision shall be null and void." Based on these two assignments, Baker must obtain prior written consents from the landlord and from Orange before Sam's can assign these agreements to our client. The risk entailed in failing to assign these to Baker is abandonment of the asset purchase.

Discussion

Both New Jersey and Third Circuit courts analyze assignment clauses using sections 317(2) and 322(2) of the Restatement of Contracts because together these provide "the best analytical framework to assess the validity of non-assignment provisions in a contract." *Owen v. CNA Ins*., 167 N.J. 450, 467 (2001); *Bel-Ray Co. v. Chemrite Ltd*., 181 F.3d 435, 441-442 (3rd Cir. 1999). Section 317 recognizes the validity of assignments, but identifies three important exceptions that limit the assignability of these rights. *See* 167 N.J. at 462. Section 322(2) is perhaps the more pertinent of these two sections because it refers to the effect of contractual provisions limiting or prohibiting assignments. By adopting this section, New Jersey follows the majority rule that contractual provisions that limit or prohibit assignments by a party only limit a party's *right* to assign the contract, but not their *power* to assign, *unless* the parties manifest specific intent to the contrary. *Id*. at 461; *See also* 181 F.3d at 442.

> (2) A contract term prohibiting the assignment of rights under the contract, unless a different intention is manifested,
>
> (a) does not forbid assignment of a right to damages for breach of the whole contract or a right arising out of the assignor's due performance of his entire obligation;
>
> (b) gives the obligor a right to damages for breach of the terms forbidding assignment but does not render the assignment ineffective;
>
> (c) is for the benefit of the obligor, and does not prevent the assignee from acquiring rights against the assignor or the obligor from discharging his duty as if there were no such prohibition.
>
> *Id*. at 460.

When deciding whether the parties intended to limit their right or their power of assignment, both New Jersey state courts and courts of the Third Circuit use the test developed by the Appellate Division of the New Jersey Superior Court in *Garden State Buildings L.P. v. First Fidelity Bank, N.A*. (Garden State test) to identify the parties' intent: "To reveal the intent necessary to preclude the power to assign, or cause an assignment violative of contractual provisions to be wholly void, such clause must contain express provisions that any assignment shall be void or invalid if not made in a certain specified way." 305 N.J. Super. 510, 522 (App. Div. 1997); *See also* 167 N.J. at 461 and 181 F.3d at 442. If the assignment clause does not contain this express language, then the parties intended to limit only their *right* to assign, and any assignment will be valid even if not done according to the terms of the contract. *See* 167 N.J. at 461 and 181 F.3d at 442. Furthermore, pursuant to § 322(2)(b), the non-assigning party has a right to damages from the assigning party for breach of the assignment terms. *Id*. If the parties intended to limit their *power* to assign, then any assignment will be invalid if not assigned as required by the provision. 305 N.J. Super at 522.

Owen v. CNA Ins. and *Bel-Ray Co. v. Chemrite Ltd*. are examples of assignments that limited the parties' right to assign. In the first case, Owen had entered into a structured settlement with a tortfeasor's insurer, Continental Casualty Corporation, following a slip-and-fall accident in a store. 167 N.J. at 452-453. Following increasing medical bills arising out of a different lawsuit, Owen assigned her rights and benefits under the settlement agreement to a mortgage and securities company, Metropolitan, without filing the required written notice with Continental. *Id*. at 453. When Continental refused to send Owen's payments to Metropolitan, Owen filed a complaint compelling Continental to declare the non-assignment provision unenforceable. *Id*. at 453-454. The Supreme Court of New Jersey, applying the Garden State test, concluded that Continental's non-assignment clause was not enforceable because it did not "reveal the intent necessary to preclude the power to assign," since it did not contain a "specific prohibition on the power to make an assignment […]." 167 N.J. at 467-470. Thus, although Owen had assigned her rights to Metropolitan without notifying Continental as required, the assignment was valid because the non-assignment provision only limited the parties' right to assign. As this involved a structured settlement, the court also analyzed the assignment clause under § 317 to assess whether Continental's material interests were affected by the assignment. *See* 167 N.J. at 469.

Similarly, in *Bel-Ray Co. v. Chemrite Ltd*., Bel-Ray, a New Jersey corporation, had entered into a series of trade agreements with Chemrite, a South African corporation, which specifically required Bel-Ray's written consent to any assignment of Chemrite's interests under these agreements. 181 F.3d at 437-438. Chemrite subsequently changed its name to Lubritene, and sold its trade agreement rights to Lubritene without obtaining Bel-Ray's written consent. *Id*. at 438. The parties conducted business in the same manner under the trade agreements. *Id*. at 439. When documents surfaced indicating that Lubritene might purposefully dissolve so as not to have any assets in case Bel-Ray chose to take legal action against Lubritene, Bel-Ray filed an action in the District Court of New Jersey to compel Lubritene to arbitrate their claims pursuant to the trade agreement arbitration clauses. *Id*. at 438-439. Lubritene claimed that it could not be compelled to arbitrate under these provisions because Chemrite's assignment was ineffective since Bel-Ray had not consented to it in writing. *Id*. at 440. The Court of Appeals for the Third Circuit held that the assignment clause did not limit Chemrite's power to assign because it did not "contain terms specifically stating that an assignment without Bel-Ray's written consent would be void or invalid," and therefore Chemrite's assignment to Lubritene was enforceable. *Id*. at 443. Therefore, Bel-Ray was entitled to an order compelling Lubritene to arbitrate, even though Bel-Ray had not consented to Chemrite's assignment in writing.

The assignment in *Garden State Bldgs., L.P. v. First Fidelity Bank, N.A.* illustrates how parties limit their power to assign, and subsequent options available to the non-assigning party. In that matter, a partnership had entered into a modification loan agreement with Midlantic Bank that included a non-assignment clause stating that any assignment without prior written consent of the other party "shall be void." 305 N.J. Super at 514-516. Midlantic assigned this loan agreement to Starwood, without obtaining prior written consent from the partnership, which began to send payments directly to Starwood. *Id*. at 517. The Appellate Division held that the partnership "had the right to invalidate the assignment" to Starwood because the assignment language evidenced "the parties' intent to render invalid any assignment that was not obtained with the consent of the other party." *Id*. at 522. Had the partnership not sent payments directly to Starwood after the assignment, it could have (1) voided the assignment or; (2) recognized the assignment but retained its rights against Midlantic or; (3) accepted the assignment and waive its rights as to Midlantic. *Id*. at 523.

Landlord Lease Assignment Clause

A court will first use the Garden State test to determine if Sam's and its landlord intended to limit their right or power to assign. Following this, it will determine whether an assignment to Baker without the landlord's consent should be void or valid.

The assignment clause in the lease provision states: "This Lease Agreement may not be assigned or subleased by Tenant without prior written consent of Landlord." This provision is similar to that in *Owen v. CNA Ins.*, and in *Bel-Ray Co. v. Chemrite Ltd*. in that it only restricts the parties' right to assign; provisions expressing that an assignment will be void without the other party's consent are absent. Thus, a court will likely conclude that this assignment clause only limits the parties' right to assign. As such, pursuant to § 322(2)(b) and the holdings of *Owen v. CNA Ins.* and *Bel-Ray Co. v. Chemrite*, if Sam's assigns the lease agreement to Baker without the landlord's consent, the assignment will not be void and Baker will be subject to all the terms in the lease agreement (similar to Lubritene and the arbitration clauses in *Bel-Ray Co. v. Chemrite*), but the landlord will be able to claim damages from Sam's for breach of contract terms. Since the landlord has complained about Sam's level of rent, the calculation of damages could include the fair market value the landlord might have received in rent for the Hackensack building had it been given the opportunity to enter into a new lease agreement with Baker.

Orange, Inc.'s Assignment Clause

A court will first decide if Sam's and Orange intended to limit their right or power to assign, and then determine whether an assignment to Baker without Orange's consent should be void or valid.

This assignment provision reads "Neither party may assign this Agreement, nor assign any of its rights or delegate any of its obligations hereunder, without the prior written consent of the other party. Any purported assignment or delegation in violation of this provision shall be null and void." Applying the Garden State test, a court will likely conclude that the parties intended to limit their power to assign because the last sentence of the assignment provision includes express language that invalidates any assignment not obtained with the consent of the other party. Consequently, because they limited their power to assign, Sam's assignment of the trademark license agreement to Baker will be invalid if

Sam's does not obtain prior written consent from Orange. The likelihood that Orange would move to invalidate this assignment, one of the options laid out in *Garden State Bldgs., L.P. v. First Fidelity Bank, N.A.*, is increased given that Orange only entered into the agreement with Sam's after carefully evaluating Sam's relevant capabilities. Therefore, Orange would most likely want to conduct a similar evaluation with any new distributor of its product.

Conclusion

Based on §322(2) of the Restatement of Contracts and the Garden State intent test, the consequences of assigning Sam's lease and trademark license agreement without prior written consent from the landlord and Orange will depend on whether the parties intended to limit their right or power to assign.

Given the holdings in *Owen v. CNA Ins., Bel-Ray v. Chemrite*, and *Garden State Bldgs., L.P. v. First Fidelity Bank, N.A.*, a court will likely hold that the lease assignment restricts the parties' right to assign because it does not contain express prohibitions on the parties' power to assign, while the trademark license agreement restricts the parties' power to assign because it does contain the required express prohibition language. Therefore, given the courts' conclusions in *Owen v. CNA Ins.*, and *Bel-Ray v. Chemrite*, the likely consequence of assigning the lease agreement without the landlord's consent is that the assignment will be valid, but the landlord will have a right to damages for breach of the terms forbidding assignment. On the other hand, given the court's holding in *Garden State Bldgs., L.P. v. First Fidelity Bank, N.A.*, the likely consequence of assigning the trademark license agreement without Orange's consent is that the assignment will be void, and Orange will move, most probably successfully, to invalidate the assignment.

To conclude, the two likely consequences of failing to obtain these prior written consents are that (1) Sam's will be liable in damages to its landlord although its lease assignment to Baker will be valid, and (2) its trademark license assignment to Baker will be void.

Memorandum

To: Partner

From: John Shindle, Marlton, NJ,
Rutgers Law – Camden, Class of 2013

Date: April 17, 2012

Re: Baker LLC-Asset Purchase from Sam's Inc.

Questions Presented

Under New Jersey law, what are the consequences of Sam's assigning a lease agreement to Baker when Sam's failed to get the prior written consent of the landlord as required in the non-assignment clause.

Under New Jersey law, what are the consequences of Sam's assigning a trademark license agreement to Baker when they failed to get the prior written consent of Orange as required in the non-assignment clause.

Brief Answers

1. A probable consequence of assigning the lease agreement is that Sam's could be found be liable for damages stemming from the assignment of the lease. Nonconforming assignments are interpreted as a breach of a covenant when the clause does not contain express provisions that the assignment shall be void if not made in a certain way. Sam's lease agreement requires prior written consent for assignments but contains no language to say the assignment would be void if that consent was not obtained. Since that language is missing, the assignment will be interpreted as a covenant not to assign and the assignment will not be void. Sam's may be liable for damages to the landlord as a result of the breach of the covenant.
2. A probable consequence is that Orange will gain the ability to void the assignment of the trademark license agreement. The non-assignment clause contains the requisite specificity in that it states any nonconforming assignment will be "null and void." New Jersey case law provides that when the word "void" is used for nonconforming assignments, the non-assigning party has the power to void the assignment. In the alternative, a possible consequence is that Orange could choose to recognize the assignment and retain its rights against Sam's as liable for any damages that result from the assignment of the trademark license agreement.

Statement of Facts

Our client Baker LLC ("Baker"), is in the process of buying Sam's, Inc.'s ("Sam's") business. The transaction is structured as an asset purchase and there are two key contracts that are important to Baker. Baker may abandon the asset purchase if those two agreements cannot be assigned. The first asset purchase is a favorable long-term lease agreement with below market rents. The second is a trademark license agreement with Orange, Inc. ("Orange") which licenses Sam's to manufacture and sell various products bearing Orange's name. Sam's generates 70% of its sales revenue from selling Orange products and as a result the agreement is very lucrative to Sam's business. Sam's has informed our client that Orange's management only entered into the agreement after a lengthy evaluation of Sam's capabilities.

The lease agreement with the landlord states that it "may not be assigned or subleased by Tenant without the prior written consent of Landlord." The trademark license agreement states that, "Neither party may assign this Agreement, nor assign any of its rights or delegate any of its obligations hereunder, without the prior written consent of the other party. Any purported assignment or delegation in violation of this provision shall be null and void."

Discussion

As requested, the memorandum will focus on the consequences of Sam's assigning the two agreements to Baker without obtaining prior written consent. The consequences of not obtaining prior written consent from the non-assigning parties differ for each agreement because of the varying language in each of the non-assignment clauses.

The language in the lease agreement does not meet the level of specificity required by New Jersey case law to warrant a voiding of the assignment and as a result the consequence of not obtaining the landlord's written consent to assignment is that Sam's may be held liable in damages for breach of covenant.

The language in the trademark license agreement has the specificity required by case law and therefore the consequence of not obtaining prior written consent from Orange is that they would likely succeed if they chose to void the assignment and preclude Baker from selling Orange products.

The *Restatement (Second) of Contracts* §322 (1981), states: (2) A contract term prohibiting assignment of rights under the contract, unless a different intention is manifested, ... (b) gives the obligor a right to damages for breach of the terms of the forbidding assignment but does not render the assignment ineffective. *Restatement (Second) of Contracts* §322(2)(b) & (c). To reveal the intent necessary to preclude the power to assign, or cause an assignment violative of contractual provisions to be wholly void, such clause must contain express provisions that any assignment shall be void or invalid if not made in a certain specified way. *Garden State Buildings v. First Fidelity Bank*, 305 N.J. Super. 510, at 522, 702 A.2d 1321 (quoting *University Mews Associates v. Jeanmarie*, 471 N.Y.S.2d 457, 461 (Sup. Ct. 1983)).

In *Garden State* the court followed the *Restatement (Second) of Contracts* §322 (1981), finding that to show the required manifestation of intent to prevent assignment, the language had to contain the result of the assignment being void or invalid if the assignment was not done in the manner agreed upon by both parties. *Id*. The non-assignment agreement in *Garden State* contained the provision that any assignment done without express written consent shall be void. *Id*. The court found that language sufficient to warrant voiding the assignment and mentioned three actions that could have been taken by the non-assigning party. *Id*. The first was option was to void the assignment, the second to recognize the assignment but retain its rights against the assigning party, and the third was to accept the assignment and waive its rights. *Id*. at 523.

New Jersey adopted the general rule that contractual provisions limiting or prohibiting assignments operate only to limit a party's right to assign the contract, but not their power to do so, unless the parties manifest an intent to the contrary with specificity. *Bel-Ray Co. v. Chemrite*, 181 F.3d 435, at 442 (3rd Cir. 1999). In the absence of such specificity, the provision limiting or prohibiting assignments will be interpreted merely as a covenant not to assign, a breach of which may render the assigning party liable in damages to the non-assigning party. The assignment, however, remains valid and enforceable against both the assignor and the assignee. *Id*.

In *Bel-Ray* the non-assignment agreement required that "express prior written consent" be given for an assignment. *Id*. at 443. The agreement did not contain the express terms specifically stating that an assignment without the non-assigning parties' consent would be void or invalid. *Id*. As a result the court determined that the clause was merely a covenant not to assign and therefore the only relief would be damages for a breach of covenant. *Id*.

The *Restatement (Second) of Contracts* §317 provides two relevant exceptions to valid assignments of contractual rights: (2) A contractual right can be assigned unless (a) the substitution of a right of the assignee for the right of the assignor would materially change the duty of the obligor, or materially increase the burden or risk imposed on him by his contract, or materially impair his chance of obtaining return performance, or materially reduce its value to him, or ... (c) assignment is validly precluded by contract. [*Restatement (Second) of Contracts* §317 (1981)]. Section 317 recognizes the validity of assignments, but specifically identifies important exceptions that limit the assignability of contractual rights. New Jersey currently uses a combined application of §317 and §322 as it believes this provides the best analytical framework to assess the validity of non-assignment provisions in a contract. *See Owen v. CNA Ins*., 167 N.J. 450, 468 (S.C. 2001).

In *CNA* the court combined the test in *Restatement (Second) of Contracts* §317 with §322 to assess the validity of non-assignment provisions in a contract. *Id*. The combination creates a subjective test that may provide some relief for those non-assignment clauses that fail to have the specific language required but for which the non-assigning party's duty would materially change or would materially increase the burden or risk imposed on them by the contract. *See e.g. id* at 468-470.

Sam's lease agreement with the landlord contains the requirement for "express prior written consent" but does not contain the provision that an assignment will be "void" or "invalid" without prior written consent. Therefore the consequence for not obtaining the landlord's signature is that Sam's may be liable for any damages that the landlord incurs as a result of the assignment.

There is no information provided which would indicate that Baker would be more likely to fail to meet the requirements of the lease than Sam's. Given that there is no evidence of a material increased burden or risk it is unlikely that a court using the subjective test would find a reason to void the assignment of the lease agreement given the finding in *CNA*. The only relief Baker need be concerned with is from their breach of the lease after the assignment. Pursuant to the case law the landlord will maintain the right to sue Sam's for damages stemming from the breach of the covenant not to assign.

Sam's trademark license agreement has the required specificity for a non-assignment clause as it states that any purported assignment without prior written consent shall be "null and void." As a result there is no need to apply the combined application framework from *CNA*. If Sam's assigns its trademark license agreement without prior written consent of Orange, Orange would likely succeed in an attempt to have the assignment voided, thereby precluding Baker from utilizing the most lucrative part of Sam's sales revenue, a main reason for the purchase.

The court in *Garden State* provided another possible consequence given the language of the clause, namely that Orange could recognize the assignment but retain its rights against Sam's as the assigning party, allowing Orange to sue Sam's for damages caused by the assignment.

Conclusion

1) The language in the non-assignment clause of the lease agreement is not specific enough because it fails to mention that any assignment will be void if done without prior written consent of the non-assigning party. The consequence of Sam's assigning the lease without the prior written consent of the landlord is that Sam's can be held liable for any damages that result from the assignment of the lease as would be the case in a breach of covenant. There is no reason to presume the landlord would succeed in a suit to have the assignment voided, under the combined application test of *Restatement (Second) of Contracts* §317 and §322, given the facts provided.
2) The language in the non-assignment clause in the trademark license agreement with Orange meets the specificity requirement of New Jersey case law as it clearly states that any assignment done without prior written consent shall be null and void. The consequences of Sam's assigning the trademark license agreement without the prior written consent of Orange is that the assignment would most likely be voided if Orange challenged it in court. An alternative consequence is that Orange could recognize the assignment and retain the right to sue Sam's for any damages that may occur as a result of the assignment, as would be the case under a breach of covenant.

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Jan. 15, 2013	5:30 p.m.	Mayfair Farms, West Orange	Joint Event with NJSCPA and Bankers Cooperative	NJSCPA
Jan. 17, 2013	4 p.m.	Crowne Plaza, Fairfield	RULLCA Seminar – North	NJICLE
Feb. 11, 2013	4 p.m.	NJ Law Center, New Brunswick	RULLCA Seminar – Central	NJICLE
March 13, 2013	4 p.m.	Double Tree Suites, Mt. Laurel	RULLCA Seminar – South	NJICLE
March 20, 2013	6 p.m.	NJ Law Center, New Brunswick	Joint CLE Meeting with Tax Law Section	NJSBA
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