ENFORCEABILITY OF CHOICE OF LAW PROVISIONS

In a recent decision, the Colorado Court of Appeals upheld a Nebraska choice of law provision found in a promissory note. The dispute centered around which state’s statute of limitations should apply to a collection action on the promissory note. Colorado’s statute of limitations for actions to collect on a promissory note is six years; Nebraska’s is only five years. Because the plaintiff filed the lawsuit approximately five and a half years after the borrower had defaulted, the resolution of the choice of law issue would decide the case.

Under Colorado law, to disregard a choice of law provision a court would need to determine that “the chosen state has no substantial relationship to the parties or the transaction and there is no other reasonable basis for the parties’ choice.” The plaintiff argued that the Denver District Court should disregard the choice of law provision and apply Colorado because (i) the loan was made in Colorado, (ii) the promissory note had been secured by property located in Colorado and (iii) neither party had any ties to Nebraska (the borrower was a Colorado resident and the plaintiff was a Wyoming company that had taken assignment of the promissory note from Bank of the West, a California bank, which had merged with the original lender). The plaintiff’s arguments convinced the Denver District Court to apply Colorado law and grant summary judgment in favor of the plaintiff.

The Court of Appeals overturned the District Court’s decision and held that the choice of law provision was binding. The Court reasoned that Nebraska had a substantial relationship to the parties because, prior to its merger with Bank of the West, the original lender was headquartered in Nebraska. Therefore, it was reasonable for that lender to choose the law of its home state to govern the transaction. The Court also relied on the fact that the lender (and not the borrower) had drafted the promissory note, thus making it fair for the lender’s assignee to be bound to its terms. In the commercial real estate context, choice of law provisions are even more likely to be enforced because courts generally presume that both parties are sophisticated enough to negotiate (and be bound by) the terms of the contract. Therefore, so long as a choice of law provision is reasonably clear, and there is some rationale for choosing a particular state’s law to govern, Colorado courts will likely enforce the provision.