Is The State A Silent Partner In Your Contract? Court Strikes Choice Of Law Provision Because Enforcement Would "Frustrate A Fundamental Policy" Of New Jersey

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"Freedom of contract", the very fabric of free market competition and the backbone of *laissez-faire* economics, stands for the proposition that every competent adult has the right to make a legally binding agreement free from governmental interference. Every contracting party engages in the process of risk allocation and valuation of economic and non-economic terms which, theoretically, results in a subjectively fair agreement, that is, an agreement that is mutually beneficial through the eyes of the parties. After all, absent fraudulent conduct, objective fairness, equity through the eyes of a stranger to the transaction, has no place in contract law. Contract interpretation cases in New Jersey often begin with the proposition that courts will not make a different or better contract for parties than the parties have chosen to make for themselves.

Freedom of contract, however, is not limitless. For example, in the early 1900's, the United States Supreme Court authored a series of decisions, beginning with *Lochner v. New York*, 198 U.S. 45 (1905), which tested an employer's right to contract with its own employees regarding such matters as hours, wages and working conditions. Agreements testing the limits of "freedom of contract" have lead to governmental regulation in numerous areas such as minimum wage, price-fixing, and unfair competition.

Recently, the New Jersey Appellate Division addressed whether parties were free to bypass a New Jersey regulatory scheme governing temporary employment agencies, in this case, an information technology ("IT") consulting relationship, by agreeing that New York law

governed their relationship. The Appellate Division answered with a resounding "No". *Softpath Systems, Inc. v. Business Intelligence Solutions, Inc.*, A-1743-11T1 (Decided January 8, 2013) involved a claim by an IT consulting company for payment for the services provided by its employees who were placed with a customer. We have previously addressed the grave consequences of IT consultant-providers' failure to register with the State under the New Jersey Private Employment Agency Act (the "Act") in our article "Of Pitfalls And Windfalls: New Jersey's Private Employment Agency Act And Its Applicability To Technology Consultant Businesses" (January 2010).[1]

In *Softpath*, the IT consulting company, a Delaware corporation registered as a New York foreign corporation with its principal offices in New York, provided IT consultants to a Princeton-based business. The parties included an explicit provision in their service contract to reflect their agreement that New York law would govern their relationship. After the client failed to pay for the IT consultants' services, the IT consultants sued for the unpaid invoices. The client sought to have the case dismissed based upon the IT consultant's failure to register under New Jersey's regulatory scheme. The IT consultant countered that New York law governs

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the parties' relationship pursuant to the choice of law provision in the service agreement and, therefore, there was no need for the New York-based IT consultant to follow New Jersey's regulatory requirements.

Affirming the trial court's order dismissing the case, the Appellate Division began by recognizing that, as a general rule, choice of law provisions are enforceable. *Softpath*, p. 8. However, under New Jersey law, a choice of law provision will not be enforced if (a) the chosen state has no relationship to the parties or the transaction, or (b) application of the law of the chosen state would frustrate "a fundamental policy of a state which has a materially greater interest than the chosen state in the determination of a particular issue." *Softpath*, p. 8 (*citing Instructional Systems, Inc. v. Computer Curriculum Corp.*, 130 N.J. 324, 341 (1992)). The Appellate Division held that the New Jersey Legislature's "primary purpose in adopting the Private Employment Agency Act was to regulate the conduct of all employees providing services to New Jersey employees and employers", and that it would frustrate the Legislature's intent to require New Jersey-based agencies to be subject to comprehensive regulation "while allowing out-of-state agencies to carry on business in this State completely unregulated." *Softpath*, p. 9 (*quoting Accountempts Division of Robert Half, Inc. v. Birch Tree Group, Ltd.*, 115 N.J. 614, 623 (1989)).

Although the *Softpath* case was decided within the framework of the New Jersey Private Employment Agency Act, the decision has broader ramifications. One can expect that anytime parties attempt to limit or eliminate a New Jersey statutory or regulatory scheme by designating a different State's laws, New Jersey courts would likely look skeptically upon such a provision. Thus, when negotiating contracts that involve regulated industries, businesses or activities, it is important to keep in mind that the State may actually be a silent party to your contract.

[1] A copy of "Of Pitfalls And Windfalls: New Jersey's Private Employment Agency Act And Its Applicability To Technology Consultant Businesses" (January 2010) can be retrieved at the following URL address: http://www.wilentz.com/files/articlesandpublicationsfilefiles/217/articlepublicationfile/pitfalls%20and%20windfalls%20final%20crop.pdf

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