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N.J. SUPREME COURT YEAR IN REVIEW

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Consumer Fraud Act Does Not Apply to 'Learned Professionals'

In response, the Legislature may amend the act to include doctors, lawyers and other licensed professionals

By Arthur L. Raynes

The Supreme Court dealt with some novel and important commercial law issues during its last term.

Limitations on Professionals' Liability

In *Macedo v. Dello Russo*, 178 N.J. 340 (2004), the Supreme Court unanimously reversed the Appellate Division with respect to whether the Consumer Fraud Act applies to "learned professionals." Plaintiffs' claimed Dr. Kellogg, who had apparently been advertised by Dr. Dello Russo as having been fully licensed when he was not, treated them. Plaintiffs did not claim any deviation from appropriate medical standards of care, but instead sought damages under the Consumer Fraud Act.

In holding that the Consumer Fraud Act applied to advertisements by doctors, the Appellate Division relied on *Blatterfein v. Larkin*, 323 N.J. Super. 167 (App. Div. 1999), and *Lemelledo v. Beneficial Management Corp.*, 150 N.J. 255 (1997). The Supreme Court in *Macedo* disagreed with the Appellate Division and rejected that court's reliance on *Blatterfein* and *Lemelledo*. In

Blatterfein, the Appellate Division held that the Consumer Fraud Act applied to an architect. The *Macedo* Court gave *Blatterfein* a narrow reading, stating that the architect in *Blatterfein* was subject to the Consumer Fraud Act for misrepresentations he made about building materials, as part of a real estate merchandising scheme, as opposed to architectural services:

In other words, although he 'happened' to be an architect, he was not functioning in that



capacity when he made false representations to induce the purchase of a house. Rather, he was operating as a real estate salesperson and that is what subjected him to the CFA. *Macedo*, 178 N.J. at 345.

In *Lemelledo*, the Supreme Court

held individuals engaged in certain loan packing practices were subject to the Consumer Fraud Act because enforcement under the Consumer Fraud Act would not conflict with the regulatory scheme of the Department of Banking and Insurance. The Supreme Court in *Macedo* rejected such a "preemption" analysis, stating that the initial issue should have been whether the Consumer Fraud Act applied to learned professionals at all. In *Macedo*, the Court held unequivocally that the Consumer Fraud Act did not.

In response to *Macedo*, the Legislature is presently considering an amendment to the Consumer Fraud Act that would subject doctors, lawyers and other licensed professionals to the act. The Assembly has passed A-2088 and the Senate is presently considering S-

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1259. The bills recognize in their text the potential conflict between legislation regulating lawyers' advertising and Supreme Court regulation on that subject.

Dickerson & Son, Inc. v. Ernst & Young, 179 N.J. 500 (2004), dealt with a limitation on professional liability with respect to accountants. Plaintiffs were 17

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food service corporations that were also shareholders of Twin County Grocers, Inc., a corporation that fashioned itself as a "cooperative." Twin County was the victim of fraud by its management, which drove Twin County into bankruptcy and liquidation.

The plaintiffs alleged they generally relied on the audit of Ernst & Young, and brought an action for accounting negligence against the firm. The Supreme Court affirmed the Appellate Division in permitting Ernst & Young to use N.J.S.A. 2A:53A-25 as a full shield against the common law claim. This statute limits liability of an accountant to third parties for negligence except when there is a 'privity' (or at least close-to-'privity') relationship. Plaintiff corporations argued that in light of the 'cooperative' nature of Twin County, they really were the clients of Ernst & Young, and not third parties. The Supreme Court rejected the argument, holding the corporations were no different from any other shareholders and their "general reliance" on Ernst & Young's annual audits was not in any event sufficient to satisfy the specific transaction requirement of the statute.

Restrictive Covenants

In *Maw v. Advanced Clinical Communications, Inc.*, 179 N.J. 439 (2004), the majority of the Supreme Court eschewed an opportunity to alter dramatically New Jersey restrictive covenant law. The Appellate Division ruled that an employee discharged for refusing to sign a restrictive covenant stated a claim under the Conscientious Employee Protection Act, N.J.S.A. 34:19-1, et seq. (CEPA). The Plaintiff claimed terminating an employee for refusing to sign a restrictive covenant states a claim because restrictive covenants implicate public policy, and therefore, could turn out to be contrary to public policy.

As a practical matter, the Appellate Division decision turned a somewhat unpredictable area of the law into a complete 'crapshoot.' In other words, a company seeking to require restrictive covenants in order to protect its per-

ceived legitimate interests would bear the risk that an employee could in the future successfully challenge the legitimacy of the covenant and hold the employer liable for damages under CEPA.

The Supreme Court majority rejected the notion that restrictive covenants constitute a clear mandate of public policy with respect to CEPA. Referring to prior Supreme Court restrictive covenant cases, the *Maw* Court stated:

The *Solari/Whitmyer* test is a multi-part, fact-intensive inquiry. Not only must multiple interests of differing parties and entities be identified, but also, those interests must be gauged for reasonableness and legitimacy. The application of that test here, and as a general matter, simply does not evoke the type of a "clear mandate of public policy" that was contemplated by N.J.S.A. 34:19-3c(3) [CEPA].

We are informed by the amici that non-compete agreements are a common part of commercial employment. We do not accept as a premise that employers, in large numbers, are engaging in a practice that is "indisputably dangerous to the public health, safety or welfare." *Maw*, 179 N.J. at 447-448. (Cits. omitted).

Justices James Zazzali and Virginia Long dissented, and would have gone far in radically changing New Jersey business practice with respect to restrictive covenants. In that regard, Justice Zazzali wrote:

I am aware of the concern by some that allowing the cause of action in these and similar circumstances might have a chilling effect on employers' legitimate use of non-compete agreements, but that argument is unavailing. The approach I propose would have the salutary effect of encouraging employ-

ers to enter into agreements that comply with, rather than flout, sound public policy. *Id.* at 459.

In *Borteck v. Riker, Danzig, Scherer, Hyland & Perretti, LLP*, 179 N.J. 246 (2004), the Court had another opportunity to address restrictive covenants among lawyers. The case marked an end to a long winning streak for departing lawyers.

The issue in *Borteck* dealt with a retirement provision in a law firm's partnership agreement. The Riker Danzig retirement provision afforded substantial benefits to capital partners who retire after reaching the age of 55 or to capital partners who retire before reaching the age of 55 provided they leave the private practice of law. Departing capital partners under the age of 55, who are appointed to the bench, assume a governmental or academic position or "engage in comparable public service work" were also deemed eligible for the enhanced retirement benefits.

The Riker Danzig provision also required that any partner desiring to retire or withdraw from the firm had to give no less than three months prior written notice.

The Court determined the retirement plan was a bona fide retirement plan and refused to find it unenforceable as against public policy. The Court distinguished *Apfel v. Budd, Larner, Rosenbaum, Greenberg & Sade*, 324 N.J. Super 133 (App. Div.), cert. denied 162 N.J. 485 (1999), in which the Appellate Division had stricken a provision limiting 'retirement' benefits to a departed lawyer. In *Apfel*, retirement was unrelated to age but was defined as ceasing to practice law within the states in which the law firm maintained an office, or becoming a member of the Judiciary. The Appellate Division in *Apfel* held the provision in that case was not a bona fide retirement clause, but merely a restraint on competition.

The Supreme Court seemed to place a great deal of reliance on Riker Danzig's retirement benefits expert, who opined that even though the Riker Danzig plan would not qualify as a retirement plan under IRS rules, its

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agreement "includes all of the normal indicia one would expect to see in a legitimate retirement plan."

As to the three-month notice provision, the Court suggested that such "provisions are not unenforceable per se." The Court referred the matter to the Professional Responsibility Rules Committee for review.

Filed Rate Doctrine

The filed rate doctrine, also known as the filed tariff doctrine, prohibits telecommunications carriers from charging rates different from those on file with the FCC. The purpose of the doctrine is two-fold: (1) it prevents price discrimination by carriers among ratepayers; and (2) it preserves the exclusive role of the FCC in approving reasonable rates for telecommunications services, and excludes courts from the ratemaking process. The doctrine serves as a bar to lawsuits against carriers when a consumer is challenging the reasonableness of its rates, or when the practical effect of a suit would result in a carrier charging rates other than those charged to other consumers. Further, a consumer is presumed to have constructive knowledge of the filed rates, and as such, is incapable of demonstrating an ascertainable loss, a requisite in filing state law causes of action for fraud or breach of contract.

Smith v. SBC Communications, Inc., 178 N.J. 265 (2004), presented an issue of national first impression regarding the filed rate doctrine. The Supreme Court had an opportunity to determine whether the filed rate doctrine would act as a *per se* bar to state law causes of action against retailers arising out of the marketing and sales of prepaid calling card services. The plaintiff purchased a prepaid calling card from a vending machine located at a BJ's Wholesale Club. The card was advertised as having a 9.9-cents-per-minute rate, i.e., a \$20 card was expected to yield 202 minutes of calling time. However, in light of unadvertised surcharges and a "round-up" practice, the plaintiff received only 50 minutes of calling time at a rate of 40-cents-per-minute.

The plaintiff filed a putative class action suit alleging claims of consumer fraud and breach of contract. The plaintiff named SNET, a telecommunications corporation governed by the FCC, and BJ's Wholesale Club, Inc., as defendants. Although the case involved a more protracted procedural history than set forth herein, SNET filed a motion to dismiss pursuant to R. 4:6-2(e) on the grounds that the plaintiff's claims were barred by the filed rate doctrine. BJ's joined in the motion and the Law Division dismissed the complaint pursuant to the doctrine. The Appellate Division affirmed the decision regarding monetary damages against SNET, but remanded the case as to BJ's. A unanimous Supreme Court held that the doctrine does not always apply to retailers, i.e., BJ's, and remanded the case to explore the relationship between BJ's and SNET.

While the case law is well established prohibiting suits against carriers, no court previously had the opportunity to consider the applicability of the doctrine as to retailers who purchase, in bulk, telecommunications services from a carrier and then offer them for resale.

In determining whether the case could proceed against BJ's, the Court looked at whether an adverse ruling against it would impinge upon SNET's filed rates. Thus, if an agency relationship existed, the retailer would be entitled to the same protections provided by the doctrine as the carrier. The Court reasoned that in such a case, the net effect of permitting monetary damages would be to effectuate a rebate for the services provided by the carrier, resulting in discrimination between ratepayers.

When an agency relationship exists between the carrier and the retailer, the dual purposes of the filed rate doctrine continue to be implicated, since the carrier then continues to remain liable for the actions of the retailer, as its agent. Unless the filed rate doctrine is enforced, "agents of the carrier might easily become experts in the making of errors and mistakes in the quotation of rates to favored [customers], while other [customers] ... whose business is less impor-

tant, would be compelled to pay the higher published rates." *Id.* at 277, quoting *Maislin Indus., U.S., Inc. v. Primary Steel, Inc.*, 497 U.S. 116, 128 (1990).

On the other hand, in the absence of an agency relationship, the Court stated that once the sale between the carrier and retailer, in accordance with the terms of the FCC filings, was complete, the retailer was free to sell the services at higher or lower rates. The Court considered the fact that the consumer had the option of purchasing the services directly from the carrier, in which case she would have paid the same rate as BJ's did. Thus, the nondiscrimination purpose was not affected. As for the nonjusticiability prong, the Court indicated that it would not be involved in deciding the appropriateness of the rates charged by the FCC, because SNET complied with its filed rates when it sold the services to BJ's.

The Court remanded for a determination of the existence of an agency relationship between BJ's and SNET. If BJ's is determined to be SNET's agent (if, for example, SNET had a hand in the misleading advertisements distributed at BJ's) then BJ's would be immune under the doctrine.

Commerce Clause

In *American Trucking Associations v. State of New Jersey*, 180 N.J. 377 (2004), the Supreme Court invalidated the state's annual hazardous waste transporter registration fee as an unconstitutional flat tax. Pursuant to the Solid Waste Management legislation, N.J.S.A. 13:1E-1, et seq., New Jersey imposed an annual registration fee on all hazardous waste transporters who collected or delivered waste in the state. The case's procedural history was extensive, but suffice it to say that the matter made its way through the Tax Court and the Appellate Division. The Supreme Court eventually remanded the matter to the Tax Court for a plenary hearing on the allegedly discriminatory economic impact of the challenged fee. The Tax Court ultimately determined that the challenged fee was invalid, and the matter returned to the Supreme Court for a

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determination of the fee's constitutional-ity.

The issue boiled down to whether the unapportioned state fee violated the Commerce Clause by discriminating against out-of-state commerce. The Court determined that the fee was not fairly apportioned — even though the same fee was imposed on each vehicle delivering or picking up waste, it had the effect of charging out-of-state transporters more per activity than in-state transporters, as the key was the “frequency with which New Jersey-based operations conduct[ed] their activities in [the] State as compared to non-New Jersey entities.”

The state attempted to argue that the fees were sustainable “user fees” pursuant to *Evansville-Vanderburg Airport Authority Dist. v. Delta Airlines*, 405 U.S. 707 (1972), and *Northwest Airlines v. County of Kent*, 510 U.S. 355 (1994). The Court, however, distinguished the constitutionally sound fees in those cases on the grounds that the imposed fees related to the payor's levels of use of the facilities or services the fees were enacted to sustain.

Statute of Frauds

In *Morton v. 4 Orchard Land Trust*, 180 N.J. 118 (2004), the Supreme Court for the first time addressed the amended version of N.J.S.A. 25:1-13, the Statute of Frauds as to the sale of an interest in real estate. “For centuries,” the law in New Jersey had been that any sale of real estate had to be reduced to writing. In 1996, the Legislature amended N.J.S.A. 25:1-13 to allow for oral transfers of real estate interests if the “existence of the Agreement” and surrounding detail could be proved by clear and convincing evidence. N.J.S.A. 25:1-13.

Morton dealt with the sale of residential property in Montclair. The parties engaged in the attorney review process and all parties seemed to agree on terms. Defendant/prospective seller withdrew from the deal when another buyer offered more money. Plaintiff/first buyer then sought specific performance. The Chancery Court granted summary judgment to the defendant and the Appellate Division affirmed. The

Supreme Court affirmed as well.

The gist of the Court's opinion was that the parties contemplated any final contract in the case would be reduced to writing. Plaintiff's proposed written contract stated that it would be binding only on “parties who sign it.” The Court distinguished *McBarron v. Kipling Woods, LLC*, 365 N.J. Super. 114 (App. Div. 2004), noting in that case the seller's attorney, Barry Jost, had repeatedly assured the spurned buyers (including in a tape-recorded conversation) that “the deal was done” and there was “definitely a contract.” The Appellate Division in *McBarron* had held that “the mere anticipation of a written memorialization of an oral agreement does not as a matter of law vitiate an oral contract.” *McBarron*, 365 N.J. Super. at 116.

The Court in *Morton* avoided an opportunity to address a conflict that it acknowledged between the Statute of Frauds, which now permits oral agreements for the sale of real estate, and the Court's own requirement that broker-prepared real estate contracts be signed by the parties. See *N.J. State Bar Association v. N.J. Association of Realtor Boards*, 93 N.J. 470, 472, 475 (1983).

Liens

In *Craft v. Stevenson Lumber Yard, Inc.*, 179 N.J. 56 (2004), an individual retained Aladich Builders, Inc., to build a house for a total cost of \$220,000. While constructing the individual's home, Aladich was working on several other projects. Aladich bought the supplies for all of its jobs from the same lumberyard, but did not delineate any of its payments to the respective projects. Thus, when the individual made his timely payments to the builder, which passed in the payments to the lumberyard, the lumberyard applied the payments to Aladich's oldest outstanding accounts. The builder eventually stopped working on the individual's property after \$166,980 had been paid. The individual contended all payments due were made. The lumberyard filed a construction lien against the individual's property for more than \$50,000 to collect

against the more than \$75,000 owed by the builder. The trial court awarded summary judgment to the lumberyard. On appeal, the Appellate Division affirmed the grant of summary judgment in favor of the lumberyard, although noting that the result was inequitable since the homeowner was forced to bear the financial burden of the builder even though he had paid the builder in full and had no knowledge of the builder's outstanding accounts with the lumberyard.

The Supreme Court addressed two issues regarding lien claims and the lien fund. The first issue was whether an innocent property owner is liable to a supplier when the property owner made payment to the general contractor for supplies, where the funds transferred to the supplier were not earmarked and the supplier did not consider the funds as satisfying the property owner's balance. On this issue the Supreme Court held it is the supplier's duty to determine which of the contractor's projects is the source of the payment and to properly allocate payments. When a supplier fails to do so, it cannot verify the existence of a debt as required under the statute and thus cannot advance a lien claim against the owner's property. The Court's reasoning was that when a creditor knows, or should know, a debtor is under an obligation to a third party to dedicate a payment to discharge a duty the debtor owes to the third party, the payment must be so applied whether or not the debtor provides specific instructions. In this case, the lumberyard knew of the individual's project because it had delivered materials there and also knew that the builder, like most contractors, is a conduit for property owners' payments. As a result, the Court found that the lumberyard knew that the payments had to be applied to reduce the property owner's particular indebtedness.

Moreover, the Court reasoned the lumberyard had a statutory duty to allocate the builder's payments to the accounts from which they were derived if it wanted to file a lien claim. A claimant can only attest under oath that a debt is owed if it maintains accurate records in which the funds received are applied to the proper accounts. Since the

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lumberyard did not allocate the builder's payments to the accounts from which they derived, it was unable to state under oath that the individual owed a debt in a particular amount and thus the lumberyard had no basis to file a lien claim.

The second issue related to the measure of the amount that is available to a subcontractor or supplier with a lien claim when the contractor abandons the project and the property owner has made all of the progress payments to date. The Supreme Court held the measure is determined in accordance with N.J.S.A. 2A:44A-10 and N.J.S.A. 2A:44A-23, by deducting the payments made to date from the total contract price the parties agreed to in writing. The Court's reasoning provided that the remedy under the Construction Lien Law (CLL) is a balancing of the interests of owners, subcontractors and suppliers by securing payment from the money the owner owes the contractor. In *Craft*, this was a critical element because the CLL limits the lien to the extent the owner is indebted to the contractor. As the lien fund was limited to the amount owed and the parties agreed that the individual did not owe the builder anything further when he walked off the job, there was no fund. The Court's holding that there was no lien fund was limited to the factual situation where a contractor abandons a job when he had been paid to date and the owner owes him no money.

In *General Electric Capital Auto Lease v. Violante*, 180 N.J. 24 (2004), an individual leased a vehicle and the title

listed the leasing company as the owner. After the vehicle was vandalized, the lessee contacted a garage keeper to make repairs to and store the vehicle. The lessee told the garage to hold off on repairs until the insurance company inspected the damage. Approximately six weeks later, the lessor sought access to inspect and remove the vehicle, because the lessee had defaulted. The garage sought the towing charges and storage fees from the leasing company, but the company refused.

The issues in *Violante* related to the Garage Keeper's Lien Act and the ability of the garage owner to get payment from the leasing company. The first issue was whether a lessee is a lessor's "representative" under the Act when the lease agreement requires the lessee to service and repair the car. The trial court concluded that the Act did not apply to leased vehicles. The Appellate Division affirmed on a different basis, finding that the garage did not have a valid lien because the lessee lacked authority to incur storage and repair charges on behalf of the leasing company. The Supreme Court reversed, holding that the obligation under the agreement to service and repair gave the lessee the power of a representative to provide the lessor's consent for services and repairs contemplated in the agreement.

The second issue was whether a garage keeper is required to notify a lessor of the vehicle's location and the amount of the charges against the vehicle to include storage fees in the lien claim.

As an initial matter, the Supreme Court noted the issue should be resolved by the Legislature, but it went on to provide "interim guidance" on the issue. The Court found the garage keeper should provide notice to the lessor and trial courts should use a test of reasonableness when evaluating the garage keeper's efforts to notify the lessor. The Court stated that notice within seven days of the vehicle's arrival at the garage is reasonable. If a garage keeper provides notice after seven days, then it will not be permitted to get storage charges incurred from the end of the initial seven-day period until the time of notification.

However, the Court further noted trial courts are to determine how much time is reasonable in the circumstances of each case, using its guidelines. In the present case, the garage keeper did not provide notice and thus was only entitled to storage charges incidental to the requested repairs. Justice Peter Verniero dissented on this part of the opinion, indicating the analysis should not have added a timeframe or notice requirement that was not in the statute and that the legislative and executive branches should address the issue.

In its analysis, the Court also noted that N.J.S.A. 39:10A-14 does not afford garage keepers with a right of recovery against lessors for costs of storage and repairs requested by a lessee. The statute is limited to situations where the vehicle is abandoned and the garage keeper has notified the owner of its intent to sell or junk the vehicle. ■